

UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF WASHINGTON AT SEATTLE

MICROSOFT CORPORATION,)	
)	
Plaintiff,)	CASE NO. C10-1823JLR
)	
v.)	SEATTLE, WASHINGTON
)	October 18, 2012
MOTOROLA, INC., et al.,)	
)	<i>Daubert</i> hearing
Defendant.)	
)	

VERBATIM REPORT OF PROCEEDINGS
BEFORE THE HONORABLE JAMES L. ROBERT
UNITED STATES DISTRICT JUDGE

APPEARANCES:

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ANDY CULBERT
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October 18, 2012

9:00 a.m.

PROCEEDINGS

THE CLERK: Case C10-1823, Microsoft Corporation v. Motorola.

Counsel, please make your appearances for the record.

MR. HARRIGAN: Good morning, Your Honor. Art Harrigan representing Microsoft, and with me this morning, starting to my left, is Mr. David Pritikin, who, along with me, will be arguing today, from the Sidley firm, and David Giardina also from Sidley; Rick Cederoth; my partner, Chris Wion; and over here we have Andy Culbert from Microsoft; and my partner, Shane Cramer; and David Kilbough.

MR. PALUMBO: Good morning, Your Honor. Ralph Palumbo for Motorola, and starting at the far end of the table is Mr. Peter Rudling, who is our paralegal in the case, and also Khue Hoang. Ms. Hoang will be arguing this morning. Jim Batchelder. Mr. Batchelder will also be arguing. My partner, Phil McCune. Mr. Jenner, who you know, who will also be arguing this morning. And then sitting in the front row, Kevin Post and Steve Pepe from Ropes & Gray.

THE COURT: Counsel, I think by my count I can see three women in this courtroom. I've never seen so many suits in one place at one time. I feel like I'm at Brooks Brothers.

Let me start with an unrelated matter, which I think you

1 will have some keen interest in.

2 You have pending a series of motions to seal, and those
3 motions to seal pertain to, I think, your *Daubert* motions,
4 your in limine motions, and your proposed findings and
5 conclusions.

6 You need to recognize that the Ninth Circuit draws a
7 distinction between dispositive motions and trials in regards
8 to sealing orders and more run-of-the-mill sealing orders.
9 And for those of you who practice in this district, you know
10 that we are not of one mind in regards to the proper approach
11 to sealing orders; that some of my colleagues feel, very
12 acutely, that we seal way too much.

13 So you are all on notice that anything that's going to end
14 up as evidence in this case, be it deposition testimony, be
15 it exhibits, be it trial testimony, will have to meet the
16 Ninth Circuit compelling interest standard, I stress
17 "compelling interest standard," or it will become a matter of
18 public record.

19 We are in the process of talking to some of the other
20 judges who have handled these cases as to how they dealt
21 particularly with the question of exhibits and trial
22 testimony. There is very, very strong authority for the
23 proposition that, short of the keys to the kingdom, I don't
24 have any ability to exclude people from the courtroom or
25 exclude public knowledge of those exhibits.

1 So when we finish processing your current batch of
2 motions, which I'm going to construe as not falling into that
3 dispositive motion standard, next time around I'm afraid
4 you're going to be entering a much higher level of scrutiny,
5 and you might want to consider that when you consider what it
6 is that you want to put into the court record.

7 Any questions about that, Mr. Harrigan, Mr. Palumbo?

8 MR. HARRIGAN: No, Your Honor.

9 MR. PALUMBO: No, Your Honor. I think we understand
10 the standard that applies at the trial.

11 THE COURT: All right. Then let's talk about where
12 we are today. We're here on Motorola's motion at Docket 393,
13 which is to exclude Murphy, Lynde, and Simcoe testimony, and
14 Microsoft's motion at Docket 396, which is to exclude Donahoe
15 and Sukumar.

16 On the very scientific basis that Motorola filed first,
17 I'll hear the Motorola motion. Why don't you assume that you
18 have 30 minutes on each side. Motorola may retain some
19 portion of that time for rebuttal. And I have some
20 questions, although less than you might think, given that
21 we've had a substantial opportunity to examine this motion,
22 and, secondly, it's a matter that has been teed up not only
23 in this case but in some other cases, so we've had the
24 benefit of various people speaking on that.

25 Any questions about the order today?

1 MR. BATCHELDER: Your Honor said 30 minutes per side?

2 THE COURT: Yes.

3 MR. BATCHELDER: Thank you.

4 My name is James Batchelder from Ropes & Gray on behalf of
5 Motorola.

6 Motorola's motion is based on what we see as four failures
7 of Microsoft's economic opinions. I'll use this slide as the
8 blueprint as we go through the presentation.

9 The first is, they are based on the wrong hypothetical
10 negotiation; the second is that they're based on a
11 negotiation that Microsoft has not reliably simulated; third,
12 they're based on a discounted patent pool benchmark that is
13 sharply biased and therefore fails the *Lucent/Uniloc* test for
14 comparables; and then fourth, they ignore the most objective
15 and reliable evidence, and they do so without justification.

16 Let's start with the first. Again, the argument here is
17 that they're based on the wrong hypothetical negotiation,
18 Microsoft's economic expert opinions. And I think to set the
19 framework, I should say that the parties agree on something
20 here, which is a rare event in this case, and that is the
21 determination of RAND range, and RAND range should be based
22 on a hypothetical negotiation, so we agree on that much, but
23 the parties' positions as to what that negotiation should
24 look like are very starkly different.

25 THE COURT: Do you agree that it's an ex ante

1 negotiation? Your motion continues to include the term "ex
2 ante," and yet you seem to accept that as part of that
3 negotiation as you model it, and, hence, I'm a little
4 confused by that.

5 MR. BATCHELDER: Well, I do think that ex ante could
6 be a useful, theoretical construct, but I think the truth is
7 that both parties, the models that they're putting forward
8 actually, in reality, have an ex post, but ex ante can be a
9 useful construct for analyzing the RANDness of the deal.

10 THE COURT: What I read in your papers was that your
11 objection here is on the multilateral level, not on the ex
12 ante level; is that accurate?

13 MR. BATCHELDER: Well, I do think that the patent
14 pool benchmark, the discounted pool benchmark that Microsoft
15 puts forward, they do it under the guise that it looks
16 multilateral and ex ante, when, in fact, it's neither. So I
17 do think it's important that even the benchmark that they're
18 putting forward doesn't meet their own criteria, and it
19 certainly, most importantly, doesn't identify or assess the
20 value of the patents being licensed.

21 THE COURT: All right.

22 MR. BATCHELDER: But back to the point about which
23 hypothetical negotiation makes sense, I do think it's
24 important to go back to how this case came to be.

25 In early October of 2010, Microsoft sued Motorola,

1 alleging patent infringement. The parties talked.

2 Microsoft -- or Motorola said we've got some patents, too,
3 and Microsoft said, well, let's put those patents on the
4 table, and then we'll have a conversation.

5 So in October -- October 10th and a little bit later,
6 also, Motorola submitted these two offer letters in October,
7 and Microsoft -- the one dealing with 802.11 and one dealing
8 with H.264, and rather than respond or negotiate, Microsoft
9 filed this lawsuit.

10 But the point is that those offer letters arose in the
11 context of a bilateral negotiation. So Motorola believes and
12 submits that the right hypothetical negotiation to
13 reconstruct here is that bilateral negotiation, that as soon
14 as Microsoft and Motorola sat down at the table and actually
15 hashed out a licensing agreement, taking into account the
16 RAND commitment, what would that look like.

17 Microsoft's position is very different. What Microsoft
18 says, and I'll show you the verbiage in a moment, what they
19 say is you have to reconstruct a very different negotiation
20 in which, for the given standard like 802.11, every single
21 SEP holder and every would-be licensee, all of them,
22 hundreds, maybe thousands, would sit down together at the
23 bargaining table and they would somehow hash out the deal.
24 It's never happened. It's pretty difficult to picture what
25 it would look like in practice given that it takes just two

1 parties in a bilateral deal probably a year or more to
2 negotiate. But anyway, that's Microsoft's position.

3 THE COURT: Let me stop you, because you're on step
4 two, and I'm still back on step one.

5 It seems to me that what you've described is an accurate
6 model of a bilateral negotiation. But in terms of setting a
7 royalty rate, I'm not sure that's what I'm asked to do. So
8 let me start with the basic question.

9 I'm supposed to study a RAND rate or a FRAND rate, both of
10 those use the terminology "RAND." What case tells me what
11 "reasonable" means?

12 MR. BATCHELDER: Well, I do think that -- if I could,
13 Your Honor, direct you to the -- invite your attention to the
14 next line. I think this begins to answer the question,
15 that --

16 THE COURT: Please answer my question, which is, I'd
17 like the name of the case.

18 MR. BATCHELDER: What I would say is that what frames
19 what reasonableness is, what the SSOs and Microsoft, and
20 indeed Your Honor and others, have said this is the framework
21 that we would look to. You know, generally, we have the long
22 line of *Georgia-Pacific* cases that talk about reconstructing
23 hypothetical negotiations between two bargaining entities,
24 and as you know from the motion that Mr. Jenner is going to
25 be arguing about, Mr. Donahoe has taken that framework and

1 modified it to accommodate the fact that he's dealing with a
2 RAND situation. But that long line of cases essentially
3 assesses how two parties do hash out reasonableness. But
4 what the SSOs tell us is that RAND negotiations are left to
5 the parties' concern, and it's because they differ from case
6 to case. That is for a given negotiation, you have to look
7 at the individual licensing entities here, Motorola and
8 Microsoft, and you have to figure out what they would agree
9 to, and that agreement is going to result in the answer to
10 your question, which is that's what reasonableness is and
11 what RAND is.

12 THE COURT: Well, if each of these is a unique
13 negotiation, what makes it unique? It seems to me it isn't
14 the fact that Motorola is on one side and Microsoft is on the
15 other. We're talking about a particular product or standard
16 and a particular patent. Is that what makes it unique?

17 MR. BATCHELDER: Well, exactly so. It's the -- it's
18 the -- the patents that are at issue; that is which ones does
19 Motorola own? How good are they? How strong are they in the
20 standard, and how strong are they to what Microsoft actually
21 does? How many products does Microsoft have that need those
22 patents to operate, and how essential are those to
23 Microsoft's business? How good of a business partner would
24 Microsoft be to Motorola? Would they want RAND factor
25 provisions, would they want defense of suspension clauses,

1 all of the kinds of things that typically get hashed out in
2 these type of negotiations. So reconstructing the
3 hypothetical negotiation, you're going to want to take all
4 that into account.

5 THE COURT: You used a word that I'm not familiar
6 with. "How strong," what do you mean by "how strong"?

7 MR. BATCHELDER: How core they are to both the
8 standard and how core they are to what Microsoft does.

9 THE COURT: Can I see if I can put some words in your
10 mouth? In other cases I have seen the language used, "what
11 does the patent contribute to the product or contribute to
12 the standard?" Do you agree that that's one of the
13 considerations?

14 MR. BATCHELDER: Yes.

15 THE COURT: And in the universe of factors, how
16 important of a factor is it?

17 MR. BATCHELDER: Well, I would submit that in
18 bilateral negotiations, which, again, I believe is the thing
19 that you want to reconstruct, that's as important as
20 anything.

21 How valuable -- if I'm the licensee, how valuable are your
22 patents to what I want to do? How many of my products
23 practice those things, and how deeply do I need your patents
24 to do it? Do your patents go to the core of the rate of my
25 products' practice, is it standard, or do they just nibble

1 around some optional stuff around the periphery? Those are
2 the kinds of things licensing parties take into account all
3 the time.

4 THE COURT: Then this is helpful for me. Then what I
5 hear you saying is if the patent contributes 75 percent of
6 the value of the standard, that would be different than if
7 the patent contributes ten percent of the value of the
8 standard?

9 MR. BATCHELDER: That's certainly true, and also it's
10 not just to the standard, but to the products that are being
11 licensed.

12 THE COURT: All right. Thank you, sir.

13 MR. BATCHELDER: So all of those things, I think,
14 would be relevant. And that's why, as the SSOs say on this
15 Slide No. 4, what if RAND differs from case to case? It
16 matters, these varying considerations that are on the
17 licensee, and it's needed for the strength of the
18 intellectual property and license. It matters very much, and
19 you need to take that into account.

20 And Microsoft had said itself the same thing as reflected
21 on Slide No. 5. They said that in RAND negotiations, you
22 negotiate on a private, bilateral basis to arrive at a
23 mutually acceptable agreement. And in the letter they
24 submitted in June to the FTC, June 2011, this formal
25 submission said, "RAND-based IPR policies provide a flexible

1 framework to help enable customized bilateral negotiations."
2 Why customized? Well, for the rare reason we just talked
3 about; that the SSOs recognize that these licenses differ
4 from case to case. So you need to take into account in
5 choosing a hypothetical negotiation what's your circumstance
6 here. And, again, the circumstance here is Microsoft and
7 Motorola in a bilateral negotiation, and we know that because
8 all of this arose in an offer letter from Motorola to
9 Microsoft, not in the context of five entities trying to sit
10 down and cross-license each other. Conceivably, a RAND
11 assessment can be made if five entities sat down to do that
12 and couldn't agree and thought that one of those entities
13 would take on a reasonable position, but that's not our case,
14 because these assessments differ from case to case. The
15 right hypothetical negotiation here is a bilateral one
16 between Motorola and Microsoft.

17 And I'd just point out Kevin Murphy, Microsoft's expert,
18 generally agrees that RAND creates this flexible framework to
19 help enable customized, bilateral negotiations.

20 THE COURT: Do I hear you saying, then, on behalf of
21 Motorola that they think the federal circuit got it right in
22 the *Uniloc v. Microsoft* case?

23 MR. BATCHELDER: I want to make sure I understand
24 which principle about *Uniloc* you're getting at, Your Honor.

25 THE COURT: They seem to be endorsing in that case

1 the same concept that you have up in whatever slide this is,
2 Slide 5, where it says you need to specialize it to the
3 details of each of the patents and standards and products.

4 MR. BATCHELDER: Well, I would submit that for a
5 bilateral negotiation, if you're going to reconstruct that --
6 and using a *Georgia-Pacific*-like analysis, you do want to
7 take into account patent value, and one way to do that is to
8 look at past licenses of the licensing entity here.

9 As you know, Motorola's *Georgia-Pacific* analysis tries to
10 reconstruct, through *Georgia-Pacific* Factor 15, that
11 hypothetical negotiation, and it recognizes that both the
12 courts and industry have long recognized that the most
13 reliable and the most objective evidence of the value of a
14 given set of patents and the reasonableness of the royalty is
15 the past licensing history of a licensor.

16 THE COURT: But I want to make sure I understand
17 that. You would agree, though, that that depends in part on
18 the end product? That's one of the considerations in that?

19 MR. BATCHELDER: The end product of the licensee?

20 THE COURT: Yes.

21 MR. BATCHELDER: Yes.

22 THE COURT: Okay.

23 MR. BATCHELDER: I want to point out Slide 6, Your
24 Honor's summary judgment order. As you say here, Motorola
25 correctly asserts that the IEEE and ITU policies contemplate

1 that RAND licenses will be negotiated between the
2 patentholder and the implementer of the standard. I think
3 that's entirely consistent with what Microsoft said in the
4 prior slide and what the SSOs have said on the slide before
5 that. It's a customized negotiation. Here, it's taking
6 place between the patentholder and the implementer. That is
7 Motorola and Microsoft, not some cast of thousands'
8 hypothetical negotiation in which everybody involved as a
9 licensor and licensee potentially for the standard would step
10 forward and try to negotiate in a melee.

11 Microsoft acknowledges on Slide 7 in its *Daubert*
12 opposition that many, even most, standard essential patent
13 licenses are the product of bilateral negotiations. They say
14 that's unremarkable and irrelevant. I believe it's highly
15 relevant in part because in reconstructing the bilateral
16 negotiation that we believe is the right one to reconstruct,
17 we have real-world examples. You have hundreds if not
18 thousands of templates that you can borrow from. This has
19 been done by thousands of licensing entities and has been
20 handled by courts for decades using the *Georgia-Pacific*
21 analysis.

22 THE COURT: Do you know of any RAND rate that has
23 been set using the multilateral approach?

24 MR. BATCHELDER: No, sir, I don't. In fact, I don't
25 feel that that negotiation that they hold out, a multilateral

1 ex ante negotiation with full participation has ever been
2 done, and their experts can't point to one.

3 All right. So here I just -- I point to Dr. Murphy and
4 Dr. Simcoe, their two experts that, again, make these various
5 points that we're trying to rely on here; that bilaterally
6 between the parties is the way to handle this kind of an
7 assessment. And, in fact, that quote from Professor Simcoe
8 at the bottom, "Hypothetical negotiation between a willing
9 licensor and a willing licensee," that's the right
10 hypothetical negotiation. When you're talking about these
11 two parties, where the dispute here arose through one party
12 offering another a license, the right hypothetical
13 negotiation to reconstruct is between the willing licensor
14 and willing licensee, not the cast of thousands they put
15 forward in their brief, and not the cast of thousands that
16 these expert opinions are all predicated on. And for that
17 reason alone, I think we need default.

18 In the interest of time, Your Honor, I'm not going to take
19 you through chapter and verse of these two quotes from
20 Dr. Lynde, but I will say that I think they help to
21 illustrate the absurdity, ultimately, of the perspective of
22 Microsoft's experts.

23 I did asked Dr. Lynde here, "Let me ask you to assume a
24 hypothetical where I, as the licensor, seek out a licensee,
25 and we agreed. We see eye-to-eye on the fact that my SEPs

1 are more valuable than the other SEPs for a given standard.
2 If we agree on that, is there anything unRAND about the
3 agreement that that licensee is going to pay me more because
4 he agrees with me that my SEPs are more valuable?" And
5 Dr. Lynde said that would violate RAND. That would violate
6 RAND because two parties can't sit down and agree. They need
7 to back up and imagine some, again, cast of thousands sitting
8 down to negotiate a license agreement, and they need to
9 imagine what that would have looked like and they need to
10 compare that to the deal they wanted to do. And only once
11 they did that can they sit down in good faith and agree on a
12 license and be comfortable that it's RAND.

13 THE COURT: Well, counsel, the trouble that I have
14 with this theme, which is rampant in your pleadings, is that,
15 while it may be accurate in an essential patent negotiation,
16 that's not what happened here. Mr. Jenner makes the point
17 every time he gets the chance that, Oh, you know, that is
18 this entity. You know, their patents and our patents and
19 this is going to be very complex and we're going to need a
20 hundred-page agreement. Yes, if you were sitting down doing
21 this as normal business people, I agree that would be
22 accurate, but you've demonstrated to the court that you're
23 not, that you're both pursuing another agenda, and therefore
24 I'm not talking about what are Microsoft's patents worth.
25 I'm talking about what is the royalty that goes with

1 Motorola's patent.

2 So this whole line of discussion that you keep pushing on
3 the court, while you need to consider the relative patent
4 strength of everyone's patent, I don't think has anything to
5 do with the question I'm being asked.

6 MR. BATCHELDER: Your Honor, if I could, that's
7 Microsoft's position; that is, that you need to take into
8 account all the would-be licensors and all the would-be
9 licensees for the entire standard, and imagine what that
10 negotiation would look like.

11 All I'm saying here is -- and you can forget about a
12 cross-license -- but if I'm a licensor and I go to a licensee
13 and I say, "I think my SEPs here are more valuable than
14 others in the industry," and the licensee says, "You know
15 what? I agree with you. I've looked at your patents. I
16 think they're more valuable, too, so I'm willing to pay you
17 more," and we enter into a deal having seen eye-to-eye on
18 that point -- Dr. Lynde here, Microsoft's expert, is saying
19 that's not RAND because you haven't imagined this melee
20 negotiation with the thousands of entities all negotiating at
21 once, even though that's never happened and it's really hard
22 to picture, that's not RAND.

23 And I would just submit that, as a practical matter, two
24 parties have to be able to negotiate like that and see eye to
25 eye.

1 Now, I grant you here that negotiation hasn't reached
2 fruition, but that happens all the time in *Georgia-Pacific*,
3 too. The parties don't agree and submit to the court, and
4 the courts reconstruct what a reasonable deal would look
5 like. And that's all we're saying here is the right
6 hypothetical negotiation of reconstruct is that bilateral
7 negotiation, even though the parties have not been able to do
8 it themselves. That's all I'm saying.

9 I would say, also, in Slide 10, when I asked Dr. Lynde
10 here was he acknowledging there had been thousands of lines
11 of SEP licensing agreements over time, and I asked him, "Can
12 you name one that's RAND?" And what he said was, "No, I
13 can't." I said, "You can't name one?" And he said, "No.
14 That would require a detailed investigation." And I said,
15 "Well, what would that look like?" And he said, "Well, that
16 could take hundreds of hours to again reconstruct this cast
17 of thousands negotiation."

18 So what are the ramifications of that position? This
19 graphic on Slide 11 is designed to illustrate these two
20 parties on the left who happily reach a deal, they both are
21 delighted with it because the licensee believes he's getting
22 patents of extraordinarily high value, and he's willing to
23 pay for that. They reach their deal, they sign it, and
24 Dr. Lynde and Microsoft's other experts over on the right
25 say, "Hold the phone. You can't take that deal because it

1 might be on RAND. We have to send this team of Sherlock
2 Holmes guys with magnifying glasses to look through the
3 multilateral full participation lens, and until we do that
4 for hundreds of hours and pay the economists to do it, you're
5 probably going to be in violation of RAND." That can't be
6 the right standard.

7 And I would submit it doesn't just put this one deal in
8 jeopardy, but it's like, well, this is designed to
9 illustrate -- it will call into question and cast a shadow of
10 doubt on the licensing agreements that have been entered into
11 under SSOs for the last 30 years. Again, that can't be the
12 right way.

13 And so, again, our first point is simply that the right
14 hypothetical negotiation here is a bilateral one, because
15 that's what the offer was. It was a one-way communication
16 from Motorola to Microsoft. It was not submitted in a pool
17 or a group, and so the negotiation they were relying upon is
18 not the right one.

19 Moving to the second very closely related point, as Your
20 Honor has already touched on. Their negotiation, they've not
21 reliably simulated, because it's never happened, to Your
22 Honor's earlier question. There never has been a
23 multilateral and standing negotiation with full
24 participation.

25 And here's Dr. Lynde's standard. This is what you need to

1 have, he says. You need to consider a multilevel, ex ante
2 negotiation with full participation, and full participation
3 is important, he explains. And I asked him in his
4 deposition, "Well, has that ever happened for a given
5 standard?" His answer: "Not to my knowledge." And none of
6 their experts have come forward with any example of this ever
7 happening, and I would submit that as a result of that, it's
8 a fundamentally unreliable exercise; and not only it hasn't
9 happened, but as we lay out in Slide 16, it couldn't happen.
10 It's forbidden by the SSOs, and, in fact, it's forbidden, as
11 Dr. Simcoe acknowledges, for antitrust reasons, because there
12 could be a group boycott if that kind of thing happens. But
13 not only has it not happened, it would likely be illegal if
14 it did happen. That renders it a fundamentally unreliable
15 pretext, and yet that is the pretext and the basic premise of
16 all of Microsoft's economic experts.

17 So moving on to the third point, they do a bit of
18 bait-and-switch. They hold up this Latin-clad standard, ex
19 ante, multilateral, full participation negotiations never
20 happened, and then they say because of all that Latin and all
21 that fancy phraseology, we're going to rely on the
22 patentholder. So they don't do the hard work to reconstruct
23 what this ex ante, multilateral, full participation
24 negotiations thing would really looked like. They say,
25 "Well, we'll look at patent pools, because we think they kind

1 of resemble that," and for a lot of reasons that fails. And,
2 again, both *Lucent* and *Uniloc* say if you're going to hold up
3 something as the plaintiff in a case and say this is my
4 comparable, you have to prove it is comparable, and they
5 can't possibly carry that burden of proof here because, in
6 fact, patent pools are sharply discounted and therefore it is
7 an extremely biased attempt at a benchmark.

8 THE COURT: Well, what would be the standard that I
9 should hold them to in terms of -- you say if you're
10 proposing a rate, what is it that you need to convince me of?

11 MR. BATCHELDER: Well, as the *Uniloc* case says here,
12 there must be a basis in fact to associate the royalties
13 rates use and prior licenses to the particular hypothetical
14 negotiation, and as *Lucent* said, "The plaintiff has the
15 burden of proof that the licenses were sufficiently
16 comparable to support the damage award." So, for example,
17 they would need to show that the royalty rate associated with
18 these patent pools, Via and MPEG LA, are not discount-house
19 royalty rates. They're royalty rates that were designed to
20 capture the fair market value of the intellectual property
21 being licensed, and here they simply cannot meet that
22 standard. And I'd like to walk you through a couple of
23 slides to help illustrate that point. I realize I'm short on
24 time, so I'll skip through some slides.

25 But I will say, just very quickly, they say multilateral

1 is important. Well, full participation multilaterally was
2 not met here. Via doesn't meet it, and they only had five
3 licensors participate in the Via pool. In the MPEG LA pool,
4 they only had 20 companies out of a thousand set the royalty
5 rate. So their multilateral, full participation criteria
6 hasn't been met.

7 Your Honor asked earlier about ex ante. The MPEG LA pool
8 was not ex ante to the formation of the standard. It came
9 six months later. And the Via pool came ten years later.
10 Clearly not ex ante. So their own criteria aren't being met.

11 And then most fundamentally they say here on Slide 22,
12 "Patent pool rates, in particular, are discounted." Here is
13 an economist, Damien Geradin, who says here, "Under a pool,
14 as part of the arrangement, members often get a discounted
15 cross-license to one another's patents."

16 So why are they discounted? Well, we list here on the
17 bottom why that is. That is, essentially these pools are
18 focusing on cheap implementation. That is, they want to
19 promulgate broad dissemination of the standardized
20 technology, and they draw licensees in with cheap rates in
21 order to get them to adopt it and adopt it broadly.

22 Why would the licensors agree to that? Because most of
23 them are implementers themselves, and Microsoft is the
24 classic example of that. They kick in their patents, MPEG
25 LA, for example, and the reason they do it is because they

1 want Windows and their other implementing products, which are
2 essentially ubiquitous in the marketplace, they're the lowest
3 cost structure possible.

4 This next bullet is very important. Patent counting
5 ignores value. These patent pools fundamentally do not do
6 what Microsoft says you have to do, and that is, analyze the
7 value of the patents. These patent pools allocate royalties
8 not by value but just by how many you've got. So if I have
9 five and someone else has ten, they get twice as much royalty
10 as I do, and if I say, wait a minute, my five patents are
11 really core to the standard and they're core to these
12 licensees' needs, my patents do exactly what their products
13 do, they're really valuable, and that guy who has ten, a lot
14 of his patents actually are nibbling around the periphery of
15 the standard, they're not what these products do. Most of
16 them look like they may be invalid anyway. The pools say we
17 don't care about that. He gets ten, you get five. That's
18 all we care about. He gets twice as much as you.

19 Antitrust scrutiny is another reason that the royalty
20 rates are low for pools, and the transaction costs are almost
21 nothing, and as a result of that, they can charge cheap
22 royalties.

23 So here is Dr. Lynde admitting -- and, again, in the
24 interest of time, I'm not going to read all the Q and A, but
25 if you have a strong licensing program, other things remain

1 the same. You're deterred from joining the patent pool.

2 And over here, even more importantly, perhaps, if you have
3 valuable patents, if you have good patents in this pool, core
4 patents, you're likely not going to want to join, because
5 it's just a patent-counting arrangement, it doesn't assess
6 value.

7 And what does that mean? If the people with the strongest
8 patents are deterred from joining, and the people with the
9 strongest length in programs are deterred from joining, the
10 ones that do join are weak. It's a discount house for cheap
11 patents for people that haven't invested in a licensing
12 program. It is not the kind of comparable that *Lucent* and
13 *Uniloc* rely upon. Microsoft cannot carry its burden here.

14 Slide 24 is about transaction costs, and again I asked
15 Dr. Lynde, "Do you agree that royalty rates can be set lower
16 in patent pools because of the reduced transaction costs?"
17 He says, essentially, yes, yes, that can happen.

18 And there's nothing on RAND, he acknowledges to the right,
19 in recovering in a bilateral negotiation the real transaction
20 costs you anticipate. So for this reason alone, these
21 discountable patent pools can't be a fair comparable for the
22 hypothetical negotiations here, which would be a bilateral
23 one.

24 Slide 25 points out that Dr. Lynde testified once in a
25 prior case about SEPs that happened to involve the 802.11

1 patent. He represented the plaintiff, and he opined about
2 the reasonable royalty there, and lo and behold, his opinion
3 was, "It was higher than the royalty rate." I asked him by
4 how much. He said he couldn't remember. I asked him if it
5 could be more than 500 percent. He couldn't remember.

6 But it's kind of ironic now that that's the rate that
7 Microsoft is trying to shove down the throat of Motorola,
8 with their own expert in a prior case saying it was below the
9 rate that was reasonable.

10 I needed to redact Slide 26 because Microsoft sealed that
11 document, but it reflects why Microsoft itself refused to
12 join the very Via pool whose royalty rate, again, it is
13 trying to shove down the throat of Motorola here, it
14 preferred bilateral negotiations.

15 And, again, for the MPEG LA, Microsoft participated there
16 and intentionally sought to suppress the royalty rate. Why?
17 Because it was very concerned with making sure that Windows
18 could be disseminated cheaply, and as they said in the bottom
19 here, "We do not foresee this patent pool ever producing a
20 material revenue stream. Revenue plays no part in our
21 decision to join the MPEG LA," and yet they're holding this
22 up as a benchmark for the fair market value reasonable
23 royalty rate when they know, they acknowledge internally that
24 it doesn't get that great of a return. It's a discount
25 house. It's not a fair benchmark. It doesn't mean the pools

1 are bad. It just means the pools are not benchmarks for a
2 fair market value.

3 And, finally, Your Honor, the last of the four independent
4 points as to why these economic expert opinions fail, they
5 ignore the most objectionable and reliable evidence out
6 there.

7 These cases, I'm not going to take a lot of time to walk
8 through them, and I'm sure Your Honor knows the case law over
9 the years has recognized what the industry has recognized,
10 and that is the best and most reliable evidence for the value
11 of a given set of patents is the licensing history of the
12 licensor, particularly if any of those licenses involve the
13 patents in suit, and, here, that's exactly what Motorola's
14 *Georgia-Pacific* type of analysis has started and stopped
15 with.

16 And the *Riles* case, at the top, in the federal circuit,
17 reversed because the district court abused its discretion in
18 failing to exclude the defendant's expert's damages model,
19 which ignored the plaintiff's established prices and practice
20 regarding royal rate, and that legal principle published in
21 the cases has been recognized by Chisum, as shown on the
22 bottom there.

23 And Microsoft's excuses for ignoring the reliable evidence
24 are, well, theoretically there could be a distinct holdup.
25 Theoretically there might be a stacking problem because

1 academic articles say that you have to think about those
2 things. And I don't disagree that you have to think about
3 them, but the question here is, do they apply in this case?
4 Is there a holdup here? Is there stacking here? And
5 definitively the answer under the evidence here in this case
6 is no.

7 We showed Dr. Lynde the statement in Microsoft's FTC
8 letter, "There is little evidence that patent holdup in the
9 standard context is a real problem," and keep in mind
10 Microsoft wrote that letter to the FTC about eight months
11 after receiving Motorola's offer letters. So we asked Dr.
12 Lynde, "Do you agree with that?" And he said, "Yeah, I have
13 no basis from the economic evidence to conclude whether or
14 not patent holdup is a real problem." And we asked him about
15 802.11 and H.264 in particular at the bottom there, and he
16 said, "Yeah, I haven't looked into whether there's holdup in
17 those industries." Well, those are the ones that matter.

18 Microsoft also says to the FTC, "Concerns about patent
19 holdup should not extend to any bilateral business agreements
20 between two companies regarding those licensing terms." Like
21 the issue here, I said, "Do you agree with that?" He said,
22 "I don't necessarily disagree with that. I don't have any
23 particular bases to disagree with it."

24 Most important -- this might be the most important slide
25 in the presentation and the most important evidence in this

1 case. We asked all three of Microsoft's economic experts,
2 "Is there evidence that any of Motorola's past licenses, one
3 that Mr. Donahoe relies upon, that any of them have been
4 affected with holdup?" And all three of them said, "We're
5 not aware of anything like that." So they waved their hands
6 and said, well, academic holdup might be a problem. Of
7 course it might be. You always have to ask. But here we did
8 ask, and their expert said, "We've got no evidence that any
9 of the Motorola licenses were affected with holdup." And so
10 what are we talking about here? Why would it be unreasonable
11 for Mr. Donahoe to look to those under *Georgia-Pacific*?

12 THE COURT: You have five minutes.

13 MR. BATCHELDER: Thank you.

14 What about stacking? If there's no evidence of holdup,
15 what about stacking? Well, we asked him that, too. Sure,
16 you have to ask whether stacking is present. The question
17 is, is it present here? And we asked Dr. Murphy, Dr. Lynde,
18 and Dr. Simcoe, and all of them said, "You know what? I
19 don't think it is present here."

20 "I don't see it in Wi-Fi or 3G," Dr. Murphy says. And
21 802.11, I asked Dr. Lynde, he said, "Not that I'm aware of.
22 It doesn't seem to be a problem in the aggregate." "What
23 about for H.264?" "I'm not aware of any studies or empirical
24 evidence about stacking there." And Dr. Simcoe: "I don't
25 have any evidence in connection with 802.11 or H.264." No

1 evidence of stacking.

2 I asked Dr. Lynde in particular, "Well, let's look at
3 these 89 patents that are SEPs for H.264 that aren't in the
4 MPEG LA pool. Why haven't those holders come to Microsoft
5 and demanded a license?" He said, "Well, I don't have any
6 information about that, but they're probably trying to create
7 implied cross-license, and that creates a de facto world free
8 license, and that could go toward solving the stacking
9 issue."

10 You would think after all this talk of stacking between
11 these two industries, Microsoft might have entered into,
12 what, a hundred licensing agreements if stacking were to be
13 an issue, at least dozens of them. The truth is, Your Honor,
14 for each of these industries, 802.11 and H.264, Microsoft has
15 entered into the grand total of one licensing agreement. So
16 MPEG LA, a grand total of one. And with Via the story is
17 even better. That is for 802.11, there are thousands of SEPs
18 outside of the Via Licensing pool. Microsoft refused to join
19 the pool, and again, it has only taken the grand total of one
20 license.

21 There is no stacking problem here with respect to these
22 industries, as their experts admit, or with respect to
23 Microsoft.

24 And then, finally, you know, we asked these experts,
25 Microsoft has publically articulated its positions and its

1 understanding from its own experience about RAND and holdup
2 and stacking. It's told the FTC what it really thinks, that
3 stacking is really more of a theoretical problem and holdup
4 is really more of a theoretical problem, and we haven't seen
5 it manifest itself in real life in these industries, and we
6 asked each of them, "Have you talked to Microsoft? Have you
7 asked them whether the opinions that you're testifying to in
8 this case square with their real life experience and their
9 opinions about these things?" And to a person, every one of
10 them said, "No." In fact, Dr. Lynde said, "I didn't even
11 know about these people. I didn't even know about the FTC
12 letter." They didn't bother to check whether these
13 theoretical handwritten opinions were grounded in the reality
14 that Microsoft has experienced.

15 Thank you.

16 THE COURT: You have reserved, at this point, two
17 minutes for rebuttal.

18 MR. BATCHELDER: Thank you.

19 MR. HARRIGAN: Your Honor, good morning.

20 Your Honor, it might actually make sense to use, as a
21 jumping-off point, the slide that counsel held up relating to
22 the Lynde testimony that he quoted, and the parts that are
23 not yellow highlighted on that slide address what we believe
24 this case is in large part about.

25 Dr. Lynde responded to the --

1 THE COURT: Which slide are we looking at, counsel?

2 MR. HARRIGAN: No. 9.

3 So what Dr. Lynde was saying about the bilateral
4 negotiations that he was being asked to address is that is
5 exactly the problem of doing ex post bilateral sequential
6 negotiations, is there are components of holdup and stacking
7 issues which are going to present a problem, and that is the
8 consistent view of not only Microsoft's experts but of many
9 other authorities and courts, and, in fact, has been
10 enunciated by Motorola itself in this case.

11 And what the -- the basic approach that Microsoft's
12 experts have taken is to identify the correct hypothetical
13 negotiation that should be used for a court to arrive at a
14 RAND rate in a standards essential patent situation, and that
15 is, first of all, it has to be ex ante, because otherwise the
16 negotiation will involve holdup, or at least there is every
17 reason to believe it will, because if you can extract more,
18 you -- generally speaking, humans figure out a way to do it,
19 and secondly, that it has to be whatever you want to call it,
20 the multilateral/bilateral decision is just semantics.
21 Multilateral, as used by the experts here, simply means that
22 you have an aggregation of licensors and licensees so that
23 you end up with a rate that doesn't -- that -- you escape the
24 problem of ending up with individual negotiations that create
25 a collection of rates that exceed the value of the

1 technology, in which case the standard doesn't work. So
2 whether you call it aggregation, multilateral, or multiparty,
3 that is the characteristic of the hypothetical negotiation
4 that our experts identify.

5 And counsel has suggested that holdup is not a problem,
6 but if you look, Your Honor, now in our notebook, at Tab 2,
7 the heading for which is "Holdup and stacking are recognized
8 concerns," the first excerpt is from Motorola's proposed
9 findings of fact.

10 "RAND commitments are designed to ensure that a standard,
11 essential patentholder will not engage in holdup. Royalty
12 stacking is another potential issue with standard patent
13 licensing." So obviously they're not imaginary concerns.
14 Motorola has proposed that the court find that they are real.

15 Their expert, Professor Schmalensee says, "RAND
16 commitments exist to address holdup. That's why they have
17 RAND. RAND is a legal requirement that's a matter of
18 contract." It's imposed in order to prevent holdup, and the
19 only way it's going to work is if, when the parties can't
20 agree on what RAND is, the court decides the issue. That
21 makes the contract meaningful and enforceable, and if the
22 court adopts the wrong approach, the one that Motorola is
23 proposing, and uses ex-post bilateral negotiation by a party
24 that is not a part or member of the patent pool, there is no
25 way to -- and now I'm going to allude to the statements about

1 the experts saying there's no evidence of holdup in
2 Motorola's negotiations. In fact, what Dr. Murphy said and
3 the others said, but Dr. Murphy specifically, I happen to
4 know clearly, said, that given human nature, you have to
5 assume that holdup is involved in that transaction because
6 Motorola has the capacity to extract that value because it's
7 not -- unless the court imposes a different result.

8 So the -- as Dr. Lynde said, the ex-post bilateral
9 negotiation cannot be assumed to yield a result that doesn't
10 have holdup in it. The hypothetical ex ante negotiation that
11 our experts are identifying as the goal you want to get to
12 assures both no holdup, and because of the aggregating
13 effect, that there isn't stacking.

14 And I'm going to now address another subject that the
15 court raised, which is, what kind of legal authority do we
16 have out there that says what RAND is? And let me start by
17 asking you to look at Tab 3 in our book, which contains two
18 quotations from the *Apple v. Motorola* case, the ones in
19 the -- the second one and the third one on the first page of
20 that tab.

21 Once a patent becomes essential, the patentee's bargaining
22 power surges, as we all know, and, secondly, the purpose of
23 the RAND requirement, and the validity of which Motorola does
24 not question, is to confine the patentee's royalty demand for
25 the value incurred by the patent itself as distinct from the

1 additional value, the holdup value conferred by the patents
2 being designated as standards and standards essential.

3 And then, Your Honor, the final quote, which I'm just
4 going to read because it's not in the book from Judge
5 Posner's decision, is, "The proper method of computing a RAND
6 royalty starts with what the cost of a licensing would have
7 been of obtaining just before the patent and invention was
8 declared essential to the compliance with the industry
9 standard, a license for the function performed by the patent,
10 that cost would be a measure of the value of the patent qua
11 patent." That's essentially -- he doesn't use the words "ex
12 ante," but that's what essentially that is.

13 THE COURT: Mr. Harrigan, let me stop you at that
14 point. It seems to me that any time I start to question
15 Judge Posner, I'm treading on dangerous ground. But let's
16 take your most recent statement.

17 What Judge Posner appears to be saying is that if I look
18 at a snapshot of time before it's declared an essential
19 patent, that that's my starting point. But at that point,
20 then, that patent is the unique property of the patentee, and
21 therefore it has a value that is attributed to the fact that
22 it is a monopoly and the patentee can exclude anyone else
23 from using it.

24 After it's declared an industry essential patent, it then
25 becomes subject to a reasonable and nondiscriminatory rate,

1 but it is available to everyone.

2 So it seems to me that, with all due respect to Judge
3 Posner, I'm not sure I agree with his view, because I'm
4 supposed to set this rate as a RAND rate and not a monopoly
5 patent rate. How do you respond to that?

6 MR. HARRIGAN: Your Honor, I agree with you, and, in
7 fact, the purpose for my quoting Judge Posner on the claim is
8 simply that it recognizes a judicial recognition of the need
9 for a so-called -- what is called an ex ante rate if you're
10 going to arrive at RAND.

11 However, he got it wrong when he picked the time, because
12 actually the time is after the standard has been adopted but
13 before it has achieved widespread adoption, because -- in
14 fact, and as our witnesses, including our fact witnesses,
15 will testify in this case, at the time, for example, that
16 H.264 had just been adopted, and the MPEG LA pool was in the
17 process of being formed, there were alternatives to H.264
18 that potentially would have won out had the patent pool not
19 gotten it right and produced a rate that was acceptable to
20 the wide swath of licensees.

21 But, Your Honor, those discussions, the fact the H.264 was
22 adopted in early '03, and the MPEG LA rates were formed in
23 the fall of '03, so that -- and, in fact, a lot of licensees,
24 as Mr. Lance [phonetic] will testify, were sitting out there
25 in the wings trying to see which way to jump and waiting to

1 see what that patent pool would do.

2 So we're going to have a substantial amount of testimony,
3 Your Honor, that the MPEG LA patent pool is the closest
4 comparable there is to the Holy Grail, which, obviously,
5 hasn't happened, but it's a hypothetical negotiation that
6 gives you a guide to where you're trying to get to. All of
7 the licensors and licensees get together at the time the
8 standard is being formed and in some fashion determine what
9 rate is the right rate for the licensors and the right rate
10 for the licensees, and they come up with a compromise that
11 reflects everybody's interests. You avoid stacking, which
12 all happens at once, and that's called multilateral, and that
13 is how you solve the problem.

14 And from the court's standpoint, the hypothetical
15 negotiation is just there to say, okay, this is what we're
16 trying to get to. I don't have one that somebody can put in
17 front of me, because if we did, there wouldn't be anything to
18 talk about, but now I'm going to look for a comparable that's
19 as close to that as there is.

20 THE COURT: It seems to me that -- first of all, I'm
21 delighting that the headline is going to be, "Microsoft says
22 Judge Posner, you're wrong," as opposed to, "Idiot judge
23 criticizes esteemed colleague," but let me go back to my
24 question, which is, in Judge Posner's analysis in *Apple*, was
25 he assuming a multilateral or a bilateral negotiation?

1 MR. HARRIGAN: Well, in his discussion, Your Honor,
2 he was assuming an ex ante negotiation, and obviously you can
3 have a bilateral --

4 THE COURT: Are you telling me we don't know which of
5 those two?

6 MR. HARRIGAN: Well, Your Honor, first of all, we're
7 talking about how the court is going to get to RAND.
8 Obviously, in the case, the parties didn't get to RAND. In
9 most cases, I believe it is correct that a bilateral
10 negotiation can take place and end up with RAND, as long as
11 the parties believe that if they don't get there, a court is
12 going to impose it.

13 But if the court uses bilateral negotiations that are
14 effected with holdup as the basis to get to RAND, then the
15 whole system is going to fall apart, because all those people
16 who were behaving inappropriately will have an incentive not
17 to do so.

18 So I don't know if I've completely answered your question,
19 but if you look at the MPEG LA situation, it has the
20 following characteristics. What I'm saying here, Your Honor,
21 is, this is not about some in-the-sky, nonexistent event.
22 This is about, in the case of MPEG LA, a very closely
23 analogous situation to that pie-in-the-sky event, and one
24 that has many other features that make it comparable enough
25 to use to arrive at a RAND royalty in this case.

1 First of all, as I said, it happened before broad adoption
2 but after the standard was adopted. Secondly, there were 20
3 licensor participants, many of whom were also licensees, that
4 included Microsoft and Motorola, both of them were both
5 licensors and licensees. When the rates were tentatively
6 published, the licensees responded and changes were made to
7 the royalties; that is, the perspective licensees who were
8 not at the table for the formation.

9 The system for MPEG LA uses a proportional allocation of
10 the total royalty among the participant licensors in the
11 pool, and that is an arithmetic fraction of the total. And,
12 Your Honor, the evidence in the case will be that neither
13 Mr. Dailey nor Motorola's expert, Taylor, can say that
14 Motorola's H.264 patents are any better than the average
15 patent.

16 So a slice of the pool that represents their arithmetic
17 share is a fair allocation for them. Obviously it's
18 comparable because we're talking about the very same
19 standard, so it's not like we're going out and looking for
20 some different set of technology. We're talking about H.264,
21 we're talking about Motorola's patent, which their own people
22 can't say are any better than the rest of the patents in the
23 H.264 standard.

24 THE COURT: It seems to me you never address what
25 seems to be the biggest distinction here, which is a pool, by

1 its very nature, is a voluntary agreement to join an
2 organization.

3 MR. HARRIGAN: Yes.

4 THE COURT: Motorola has stated it doesn't want to be
5 in the pool. It wants to go it alone and it wants to
6 negotiate based on that position.

7 So, I mean, how can I take something which is a
8 fundamentally different character and say it controls a
9 completely different situation?

10 MR. HARRIGAN: Well, Your Honor, there are a couple
11 of ways -- there are a number of reasons why that works.
12 First of all, it's certainly true that Motorola was under no
13 obligation to join the pool. But the court needs to find a
14 closely comparable situation to arrive at a rate, and a rate
15 where the situation has the characteristics of, at least if
16 not completely ex ante, at least as close as we're going to
17 get, because it's before widespread adoption.

18 And so the rates that those parties agreed to in the pool
19 are very likely to be in the right order and magnitude,
20 subject to adjustment; for example, if Motorola came forward,
21 which it can't, and said that its patents were more valuable
22 than the rest. But the fact is, they aren't, and what we're
23 talking about here is a standard and what is -- in effect,
24 what is Motorola's proper share of a reasonable total royalty
25 for that standard?

1 THE COURT: Well, but -- go back to the fundamental
2 question here.

3 The motivation of someone joining the pool and setting a
4 pool rate is not the same as Motorola's motivation, which is
5 to maximize its return.

6 MR. HARRIGAN: Well, Your Honor, the motivation of
7 the licensors in the pool is to make the standard work, and
8 the way to do that is to come up with a rate that is high
9 enough to give the licensors a return that they believe is
10 fair and adequate without going so high as to deter the many
11 licensees that you want to have sign up from signing up.

12 And, Your Honor, this particular example is
13 particularly -- is especially compelling, because what
14 actually happened is that Motorola participated throughout
15 the formation of the MPEG LA pool. It argued for lower rates
16 than were initially discussed, it argued for lower caps than
17 initially discussed, and it entered to and agreed to and
18 signed off on two press releases from MPEG LA stating these
19 are our rates, and then right before the pool was formed,
20 Motorola decided to drop out.

21 But you'll have unequivocal and undisputable evidence that
22 it agreed with the ultimate rates. And, in fact, part of the
23 reason they were what they were is because Motorola argued
24 that they should be lower than those initially discussed.

25 The other point, Your Honor, that I think is important is,

1 if you look at Tab 5 of the notebook, the notion which
2 Motorola has repeated several times in its argument this
3 morning, that the pool rates are super cheap, is refuted by
4 their own expert, Mr. Smith, who, at Tab 5, said, "This is
5 not to say that patent pools seek to promote downstream
6 manufacturing through low royalty rates at the expense of the
7 patentholder or licensors. Rather, the pool royalty rates
8 must be set to balance the desire to attract licensees with
9 the need to attract other potential licensors. If the rates
10 are too low, not enough licensors will join the pool."

11 So, Your Honor, I'm not saying that this is the perfect
12 comparable, but it is a very compelling comparable, and it's
13 a landmark the court can use to arrive at a rate, and we
14 believe that the rate will be in the same neighborhood as the
15 pool arrived at, because, Your Honor, that pool replicates
16 the ex ante situation that we want to get to, and it
17 replicates the situation where you do not have, a, after the
18 fact, a bilateral series of negotiations, each of which
19 extracts holdup so that the total cost of implementing the
20 standard is a higher cost than two reasonable sets of people
21 would ever have agreed to when it was in the process of being
22 put together.

23 And when you're dealing with standards, that has to be the
24 goal, is to get to the rate that -- if you had a bilateral
25 negotiation of all the licensors and all the licensees, you

1 would get a rate that was in the middle of what it took to
2 attract both of them and avoided making the standard too
3 expensive for the licensees. That's what you would get.

4 THE COURT: Has there before been such a multilateral
5 negotiation?

6 MR. HARRIGAN: Your Honor, I don't think -- we cannot
7 cite that to you, but that very subject --

8 THE COURT: I take it that was a "no."

9 MR. HARRIGAN: Right. But it's important to qualify
10 that by saying that the IEEE and other standards
11 organizations are currently discussing doing that very thing.
12 But, Your Honor, here's the problem. I mean, I -- but right
13 now we don't have that system. Obviously if we had that
14 system, there wouldn't be any need for judicial intervention
15 because all the rates would be set by contractors in advance
16 for everybody.

17 Here we have a system that depends on the parties agreeing
18 to a RAND rate, and the licensor is offering a RAND rate
19 whether they're in a pool or not in a pool, and the court's
20 problem, of course, is, how do I figure out what that is when
21 the parties can't agree? And all I'm saying is that a pool
22 that is formed with a large number of licensors involved and
23 is accepted by a large number of licensees and occurs close
24 to the time when the standard was adopted, before there was a
25 holdup potential, is a very good comparable.

1 And, of course, Your Honor, this is a *Daubert* motion.
2 There doesn't have to be a perfect comparable. That's a
3 question of how much weight the court chooses to give it.
4 But it is a piece of evidence that our experts are relying
5 on, and they should be entitled to rely on it.

6 Let me go back to where we -- you know, kind of a legal
7 issue here.

8 Motorola basically makes two arguments; one is the
9 standards organizations require bilateral negotiations, and
10 I'm not going to read through this, but if you look at Tab 1
11 of our notebook, we have put there all the quotes in
12 Motorola's brief from the standards organizations on this
13 issue that they -- on pages 4 and 5 of their brief, and you
14 will not find a single statement in here that even requires
15 the parties to engage in bilateral negotiations, much less
16 when to tell the court how to go about setting a RAND rate.

17 So we are not operating under some mandate for the
18 standard-setting organizations here to use only bilateral
19 comparables. In fact, the whole notion of bilateral versus
20 multilaterals, as I said, is just semantics, because you can
21 have a bilateral negotiation with three licensors on one side
22 and three licensees on the other side, and lateral means
23 side, it doesn't mean how many people are on each side. So
24 there is nothing here in the -- the standard-setting
25 organizations are not controlling this situation.

1 THE COURT: Well, since we're on this topic, can you
2 point me to any RAND rate that has been set by a court, using
3 your proposed multilateral negotiation model?

4 MR. HARRIGAN: I don't think there is a RAND rate
5 that's been set by a court, Your Honor. I think that's the
6 reason that this is a very important case, because this case
7 is going to determine how that's done.

8 THE COURT: All right. So the answer to that one was
9 no. Then let me take you to part two, which is, can you
10 point me to any rate that's been set using this multilateral
11 negotiation?

12 MR. HARRIGAN: Yes, the MPEG LA rates for H.264.

13 THE COURT: That's the one you would -- I hate to say
14 "hang your hat on," but --

15 MR. HARRIGAN: Yes, Your Honor. And, in fact, the
16 Via pool on 802.11 is not as strong a comparable as the MPEG
17 LA pool, but, in fact, the Via pool was formed at or before
18 802.11 became very widely adopted. And so it's -- it is a
19 data point that should be considered here along with other
20 data points in arriving at a RAND rate there.

21 So -- but I think that the answer to your question is the
22 MPEG LA pool is very close to -- it is -- it is ex ante.
23 What it isn't is, it's not fully multilateral, but it's very
24 substantially -- it includes a large number of the people
25 involved.

1 And, you know, Your Honor, so the only prong of Motorola's
2 argument besides the invalid one that the standard-setting
3 organizations forbid nonbilateral activity is that the
4 economic theory doesn't stack up in this way. And the fact
5 is that Motorola itself has advocated this very thing.

6 If you look at Tab 4, this is a submission in 2006 by
7 Motorola to ETSI, which is a telephone standard-setting
8 organization in Europe. And Motorola -- the second page,
9 actually, should be the first page. If you look at the
10 second page of this tab, Motorola was worrying about
11 cumulative royalties, which were often uncertain, possibly
12 too high, and, at worst, prohibited. And multitechnology
13 purpose devices complicate the picture. And, finally,
14 licensors could push royalties up in an unlimited way. That
15 was what Motorola was worried about, and its solution was to
16 use what it calls the aggregated reasonable terms approach.
17 Essentially, patent owners agree to grant licenses on terms
18 that are objectively and commercially reasonable, taking into
19 account the overall licensing situation, including the cost
20 of obtaining all necessary licenses from other relevant
21 patentholders for all relevant technologies in the end
22 product.

23 And then as far as distributing the royalties, they
24 advocated proportionality, and they said these proposed
25 changes are really in the nature of clarifications of

1 existing RAND rules and commonly understood goals.

2 So Motorola agrees that stacking is a problem, Motorola
3 agrees that holdup is a problem, and they advocated something
4 that sounds an awful lot like an ex ante multilateral
5 negotiation to solve those problems.

6 And opposite this, we have put Mr. Simcoe's statements,
7 which you'll see bears a close resemblance to what Motorola
8 was advocating in 2006.

9 In addition --

10 THE COURT: Mr. Harrigan, before you run out of time,
11 one of the tests that I'm obligated to apply is the
12 reliability standard under *Daubert*. Given that this has
13 never happened, how can I find that it's reliable?

14 MR. HARRIGAN: Well, Your Honor, the hypothetical
15 negotiation that *Georgia-Pacific* calls for has never
16 happened, either. That's a hypothetical negotiation that
17 includes a bunch of legal requirements, such as the entire
18 market rule, that the parties -- bilateral negotiating
19 parties are not bound by it, but it is a hypothetical
20 situation that exists as a way of measuring patent damages.

21 So the fact that it's never happened is -- Your Honor,
22 we're not asking the court to make believe something happened
23 and then adopt it. We're saying if you're looking for what
24 the RAND royalty needs to be, you look at a hypothetical
25 situation just like the *Georgia-Pacific* hypothetical

1 situation, and it has certain characteristics. Then you look
2 for a comparable real-world situation that closely
3 approximates the ideal. But as an economic theory matter, it
4 makes sense to first posit what the ideal is. And, in fact,
5 Motorola's own experts have said that that is a good way to
6 get there.

7 THE COURT: Mr. Harrigan, I think you fundamentally
8 misunderstand the relationship between the district court and
9 the courts of appeal, and in particular the federal circuit.
10 They validated the *Georgia-Pacific* approach hundreds of
11 times. You know, this court employs it regularly in patent
12 cases. I mean, it's been found reliable, producing reliable
13 results.

14 What you're telling me is, this is the best approximation
15 there is out there, but it's never been used, so you should
16 consider it, but, you know, we can't really vouch for the
17 accuracy of it.

18 MR. HARRIGAN: Well, Your Honor, what we can vouch
19 for the accuracy of is the proper comparables. The evidence
20 of Motorola's, in effect, admission that the MPEG LA rates
21 are appropriate. And, Your Honor, this is the first time a
22 court is going to set a RAND rate, so I think it's not any
23 mystery that this court is going to have to determine how
24 that is done, and that may be the RAND version of the
25 *Georgia-Pacific* case. But there isn't an appellate court

1 that's ever said how you do this, because it hasn't happened
2 before.

3 THE COURT: Well, in my chambers it's very easy. We
4 refer to it as the Fortney doctrine. That's an inside joke
5 for those of you who know my law clerk.

6 MR. HARRIGAN: Your Honor, I would just call your
7 attention to the fact that Mr. Schmalensee, who is one of
8 Motorola's experts in this case, has written a paper, which
9 we've cited in our papers, in 2007, in which he advocates
10 figuring out a RAND rate by using a hypothetical series of
11 auctions, in effect in which the licensors bid for the amount
12 that they would take for their technology to be included, and
13 that that is part of the process of determining whose
14 technology gets included, but the net result is you end up
15 with the best technology and for a reasonable sum that
16 represents the actual value of that technology because of the
17 auction. And that auction approach is essentially the same
18 thing as the multilateral, hypothetical negotiation. It's a
19 hypothetical auction, which is a form of negotiation, and
20 it's certainly not bilateral because it involves licensees
21 and licensors negotiating.

22 THE COURT: The academy, the last refuge of desperate
23 people.

24 Why don't you go ahead and wrap up, counsel.

25 MR. HARRIGAN: So, finally, Your Honor, I guess the

1 other part of this, given this is a *Daubert* motion, is, we
2 can't figure out what Motorola is trying to exclude. I guess
3 they don't want the experts to say "multilateral." I don't
4 think they can, with a straight face, say they can't say ex
5 ante, because it's clear it has to be ex ante to avoid
6 holdup. So if our experts aren't allowed to use
7 "multilateral," we can live with that, but their analysis is
8 an accepted and recognized economic framework for arriving at
9 RAND, and we have abundant evidence of comparable situations
10 in the real world that enable the court to figure out
11 approximately what that hypothetical ex ante negotiation
12 would have produced. And that, we believe, is the correct
13 way to arrive at RAND, and that using after the fact
14 bilateral negotiation, which inevitably involves the holdup
15 potential, it is the wrong way to proceed, because it will
16 result in higher rates, stacking, and holdup, if that
17 approach is endorsed by the court, because there will be an
18 incentive for people to charge -- to do what Motorola has
19 done.

20 The other -- and, finally, Your Honor, the best evidence
21 here of, I guess, holdup in Motorola's behavior is that its
22 approach has been in this case to ask for and demand a very
23 high royalty, and then when the other party doesn't accept
24 it, go to Germany to get an injunction in order to give them
25 an incentive to give in, and that's another element of

1 behavior that needs to be deterred and in which a RAND rate
2 setting process that arrives at the ex ante value will
3 prevent.

4 Thank you, Your Honor.

5 THE COURT: Thank you.

6 Mr. Batchelder, Mr. Harrigan gave you a launching pad for
7 one of the court's questions.

8 It seems to me that many of your slides go to what's wrong
9 with this expert's testimony, and that's the question that
10 arises in the *Daubert* motion. But, you know, I guess I'm
11 still at a loss to understand. Is Motorola also contending
12 that patent pools are a bad comparable, or is just the
13 testimony of these experts in regards to a specific patent
14 pool improper?

15 MR. BATCHELDER: The latter, Your Honor. That is,
16 the line here on these two patentees, they have not carried
17 their burden of demonstrating that they are comparables as
18 the federal circuit requires, the showing of proving a
19 comparable under the *Uniloc* and *Lucent* standards.

20 I don't mean to say that no pool anywhere, no matter how
21 it gets royalties, could ever be thought of as a comparable
22 for any other kind of license. But here, given it's a
23 bilateral, hypothetical negotiation that you need to
24 construct, Your Honor put your finger on exactly the problem.
25 These pools are, as Your Honor said, a fundamentally

1 different character; that a one-on-one negotiating license
2 agreement, as Your Honor correctly pointed out, the
3 motivations of the people that join pools are fundamentally
4 different than the motivations of someone licensing in the
5 real world who wants to sit down and get fair market value
6 for their patents. They cannot meet that standard.

7 Mr. Harrigan said, well, what the court needs to do is to
8 find a closely comparable situation. Well, that's exactly
9 what Mr. Donahoe has done.

10 The close comparable in the *Georgia-Pacific* case, he
11 turned to the licensor and said, "Do you have a licensing
12 program that's well established? Do you have patents" --
13 excuse me -- "do you have licenses that cover these patents
14 in suit?" If so, that's the first place you go to.

15 THE COURT: You're getting into, I think,
16 Mr. Jenner's defense here in a moment, so let's stay on path.

17 MR. BATCHELDER: Okay. So coming back to patent
18 rules, I think as I've gone through, Your Honor, there's
19 abundance evidence here that they are essentially discount
20 houses, that their -- it's to broadly disseminate the
21 standardized technology, which is great, that serves a useful
22 function. But one function these patent pools can't serve is
23 the fair comparable for fair market value of the given set of
24 patents. That they don't do in a bilateral negotiation.

25 THE COURT: Why is your comparable analysis only in

1 your rely brief?

2 MR. BATCHELDER: I believe that we touched on it in
3 our motion, too, Your Honor. I'd be happy to fetch it and
4 find the passages I think are relevant to that. But I think
5 it straddles both parts. The point of -- essentially we made
6 the argument on the multilateral ex ante motion, and they
7 came back and said, well, there could be holdup, and you
8 should look to pools, and in response to that we said, well,
9 you haven't proven all of the pools, and the pools you're
10 pointing to are not good comparables, so it kind of comes in
11 that logical progression.

12 The other fundamental point that you made, and you put
13 your finger on exactly the problem: *Daubert* and 702 are
14 about reliability, and their economic construct, all of their
15 opinions are predicated on, are based on a negotiation that
16 has never occurred, and therefore cannot reliably
17 reconstruct. Whereas in contrast, *Georgia-Pacific*, for
18 decades, as Your Honor pointed out, has been reconstructing
19 hypothetical negotiations between two licensing entities, and
20 here we have a great body, and the fact those kind of
21 license -- like Motorola and other sophisticated licensees
22 like Nokia and like RIM and like Datech that establish a good
23 baseline.

24 I do just want to point out, Mr. Harrigan did question
25 whether Microsoft's experts really did say that there was no

1 evidence of holdup. And just as one example, I have
2 Dr. Lynde's deposition here, and I just want to read to you
3 from page 34, line 1 through line 6. I handed him Exhibit C
4 to Donahoe's report, which is 50-plus licensing agreements
5 that Motorola has entered into that he was turning to for his
6 *Georgia-Pacific* comparables, and that was Exhibit 13 to the
7 Lynde deposition. I said -- I'm just reading from the
8 transcript. It's not a separate slide.

9 "Looking at Exhibit 13, my question is, are there any
10 agreements on this exhibit as to which you have any specific
11 evidence that holdup was involved."

12 "ANSWER: With respect to these agreements, I do not have
13 specific evidence."

14 So Microsoft's experts, they had these agreements, they've
15 been able to take discovery, they're heavily incented to find
16 evidence of holdup associated with them, they have nothing,
17 they have nothing at all, and it's not good enough to come in
18 here and say holdup is an economic possibility. You have to
19 show that holdup matters in this case on these facts, and
20 they've got the facts and they've got the licenses, and they
21 haven't been able to point to any. Neither have they been
22 able to point to any evidence of stacking, because, again, in
23 each of these industries, Microsoft has taken a grand total
24 of one license. There cannot possibly be any stacking.

25 THE COURT: Counsel, we'll take our morning break at

1 this time. We'll be back at a quarter to 11:00, and we'll be
2 taking up Microsoft's motion at that time. We'll be in
3 recess.

4 (A RECESS WAS TAKEN.)

5 THE COURT: Who is going to be speaking for
6 Microsoft?

7 MR. PRITIKIN: I will, Your Honor.

8 THE COURT: All right.

9 MR. PRITIKIN: We talked to Motorola's counsel, and
10 we suggested it might make sense for us to break out the
11 Donahoe and Sukumar portions of this, argue Donahoe through,
12 and then Sukumar, we have different lawyers doing the
13 arguments, and we anticipate the Sukumar argument will be
14 quite short anyway.

15 THE COURT: All right. Is that acceptable,
16 Mr. Jenner?

17 MR. JENNER: Yes.

18 THE COURT: All right.

19 MR. PRITIKIN: As Your Honor is aware, Mr. Donahoe
20 purported to employ what he called a modified *Georgia-Pacific*
21 analysis. What he did not do is to say how he modified
22 *Georgia-Pacific*, why he modified it, where he found some
23 precedent for the authority for the modifications that he
24 proposed to make. And, in fact, if one looks at the
25 testimony of their economist, Schmalensee, and contrasts that

1 with the testimony of Mr. Donahoe, that they're basically
2 crossing each other where neither comes up with some kind of
3 economic rationale, some logic for the modifications that
4 have supposedly been made.

5 Now, we know that no court has ever, ever used a modified
6 *Georgia-Pacific* analysis to determine a RAND royalty or, for
7 that matter, any other kind of royalty.

8 Beyond that, I think the place to start is what is
9 *Georgia-Pacific* anyway? And there is a misunderstanding, a
10 misconception about what it really is.

11 *Georgia-Pacific* is not a test, it is not an analytical
12 framework, it is a non-exhaustive list of factors that can be
13 considered in patent damages.

14 Now, I have a handout, and let me -- may I hand up a
15 couple of copies of this, Your Honor?

16 THE COURT: Yes.

17 MR. PRITIKIN: What I've done here, Your Honor, is
18 primarily quotations, and I've numbered the paragraphs so
19 that we can refer to them as we proceed through the argument.

20 The first paragraph that we have is a statement by Chief
21 Judge Rader from the federal circuit, who was talking
22 recently about *Georgia-Pacific*, and what he said is, he often
23 bristles when he hears people talk about the *Georgia-Pacific*
24 analysis, because he says it's really just a laundry list of
25 various things to be considered. The factors were never

1 meant to be a test or a formula for resolving damages issues.
2 They're merely a list for things to consider, and that's
3 clear from reading the *Georgia-Pacific* case itself.

4 What experts often do in patent damages cases is come up
5 with some number, a royalty rate, walk through the
6 *Georgia-Pacific* factors, and then have a thumbs up or a
7 thumbs down on each factor, this would put it up, this would
8 push it down, this one is neutral, and that was the way a
9 number of people approached this.

10 But in the recent federal circuit decision of *Whitserve*,
11 the federal circuit made clear that is not an acceptable
12 approach to using the *Georgia-Pacific* factors. It is a list
13 of things that may be considered, but what is required is
14 real economic analysis and not simply a cursory or conclusory
15 recitation of whether a factor will move a rate up or down or
16 leave it neutral.

17 I'll come back to this a little later, but that's really
18 one of the flaws, a methodological flaw that permeates what
19 Donahoe has done here.

20 THE COURT: Did the Western District of Washington
21 move to the federal circuit?

22 MR. PRITIKIN: No, sir.

23 THE COURT: Then why do I care what they say?

24 MR. PRITIKIN: Because the federal circuit case law
25 on patent damages provides useful information in connection

1 with the RAND determination.

2 THE COURT: Can you cite me to a Ninth Circuit judge
3 that said that?

4 MR. PRITIKIN: I can't, Your Honor. There was a
5 time, of course, where the appeals went to the regional
6 circuits in patent cases, and it may be possible, I suppose,
7 to canvass the whole Ninth Circuit law on it.

8 But what the court is tasked with here is determining what
9 a RAND royalty is. I mean, that really is what we're up to
10 here.

11 THE COURT: We all agree upon that. But due to the
12 unique procedural posture of this case, and we all learned
13 the other day, it goes to the Ninth Circuit, and the last
14 time I checked, the Ninth Circuit was not saying we blindly
15 follow the federal circuit. And so, therefore, I'd ask both
16 sides to concentrate on what the Ninth Circuit law is,
17 although I'm the first to tell you that it's sparse, and it's
18 going to be particularly sparse in regards to RAND rates
19 because that's not what they normally do. But they are very
20 experienced in a lot of other areas, and they have
21 *Georgia-Pacific* cases.

22 MR. PRITIKIN: Correct.

23 And, Your Honor, I think to the extent we're going to be
24 looking to federal circuit law, we're going to look to it as
25 I think the Ninth Circuit would look to it, which is that

1 there is a large body of law there that deals with the
2 question of reasonable royalty in the context of patent
3 damages, and it may be helpful, it may be persuasive, it may
4 be illuminating, you're correct, Your Honor, it would not be
5 binding on the Ninth Circuit. We're to look to that simply
6 for the persuasive value that those cases are going to
7 provide.

8 Now, returning to what it is that Donahoe did, he did
9 purport to follow at least some form of federal circuit
10 damages law with *Georgia-Pacific*, but modified it in some
11 way, and as I said, there's no precedent for determining RAND
12 royalty the way he did it.

13 But there are at least four methodological flaws in what
14 it is that Donahoe did. The first is that in selecting the
15 two-and-a-quarter-percent royalty that he used, and that was
16 both his beginning and his ending point of the analysis, he
17 did not apply a reliable methodology in picking that number.
18 He purported to base it on what he called "comparable
19 licenses," but he didn't do that, and all you have to do is
20 look at his report to see he didn't do that.

21 The second problem is, that to the extent that he
22 purported to apply *Georgia-Pacific* and that he used that to
23 validate the framework in which he was using, he recited
24 those factors without any analysis or economic explanation or
25 quantification of how they influenced what he considered to

1 be a reasonable royalty.

2 Third, he applied a percentage royalty to the entire value
3 of the products, like Xbox and Windows, without any
4 apportionment. And, again, the entire market value rule is
5 something that has been developed in the context of patent
6 damages for determining a reasonable royalty. We think it is
7 highly persuasive because the fundamental principle
8 underlying it is that it is designed to prevent the patentee
9 from getting a windfall on things that he did not invent.

10 And, fourth, Donahoe failed to follow an accepted
11 methodology, because the way he designed this modified
12 *Georgia-Pacific* approach, he set out to capture the holdup
13 value and not the value of the Motorola patents.

14 Now, I want to talk about each of these in a little more
15 detail.

16 Let me start with the two and a quarter percent that he
17 used both as his starting point and his ending point in his
18 analysis, and the threshold reliability of the entire
19 analysis that he did is going to turn on whether or not he
20 had a proper starting point, because that was both the
21 beginning and the end of the analysis.

22 He based the two and a quarter percent primarily on past
23 licenses to Motorola's cellular telephone network patent
24 portfolio. Now, we heard earlier this morning talk about how
25 they had used comparables. These were different portfolios.

1 Motorola had patents that they said were essential to various
2 cellular standards, the standards that are used when you make
3 cell phones.

4 There has been no demonstration at all, by Donahoe or by
5 any of the other experts, they didn't even attempt to show
6 it, that there was any comparability between the patents that
7 are essential to a cellular standard and those that are at
8 issue here.

9 Now, many of these involve licenses just to the cellular
10 portfolio, and there are over 100 Motorola patents that they
11 had said are essential to the cellular portfolio and licenses
12 for those implementations.

13 Now, how is it, then, that Donahoe said it was all right
14 to rely on these licenses to the cellular patents? The
15 rationale that he has come up with is that there are some
16 patents that are in common or overlap between the cellular
17 portfolio and the 802.11 wireless portfolio. There's no
18 argument that the H.264 patent, that we have any commonality
19 there, just the wireless. And you'll often see when you read
20 through the papers that they filed, the patents are licensed
21 in both, plural. But we can cut through all that and really
22 focus on what the facts are here.

23 And if you turn, for example, Your Honor, to paragraph 5
24 in the handout that I provided to the court, these are
25 excerpts from Motorola's proposed findings of fact that was

1 filed with the court, and what Motorola has said, if you look
2 at paragraph 210 of the findings, that there are -- I believe
3 there are nine patents listed there that they say are used by
4 Xbox. That's the product they pointed to using the 802.11
5 standard. So whittling this universe down, there really is
6 only these patents. This is what their case is based on.

7 And then if you look further back in their proposed
8 findings, 436 to 439, you can see their discussion of the
9 other license agreements, those agreements that involve the
10 licenses to the cellular portfolios, and what you see when
11 you compare these is that there are two 802.11 patents, just
12 two that they say are always licensed for use in a cellular
13 implementation. Now, that is two patents out of over 100 in
14 the cellular portfolio.

15 Donahoe is pointing to those cellular licenses and saying
16 they somehow inform what a royalty would be for the 802.11
17 patents, but a point in fact, when you actually look at what
18 Motorola is contending here, the overlap is vanishingly
19 small, it is two patents, there's never been an apportionment
20 of those two, and those two patents that they pointed to are
21 licensed for use in a cellular implementation, not for use in
22 an 802.11 implementation.

23 And so the argument that somehow because there is some
24 commonality of one patent or two patents, that that would
25 justify looking at the cellular portfolio as a comparable,

1 simply disappears.

2 If we look at paragraph 6 in the handout I provided, you
3 can see that Donahoe hasn't even attempted to make the kind
4 of apportionment that would be necessary.

5 So when you actually look at all of the Motorola licenses
6 that they're relying on, that they try to use to say that
7 there is something comparable here that would justify using
8 the two and a quarter percent that they started with, in the
9 end it really comes down to one license. And it talked
10 about, in paragraph 7, Motorola has designated all of this as
11 confidential, so I don't want to say it on the public record,
12 but as you can see, the amounts are so small that they
13 plainly would not satisfy anybody's requirement or showing
14 that there's any kind of an established rate here.

15 Now, there are further problems in the attempts that
16 Motorola has made to try to use these licenses to establish
17 some kind of comparability. We know that they involve
18 different patents, different standards, but they also involve
19 different licensed products for different purposes. Common
20 sense tells you that in order to have a cell phone, you're
21 clearly going to need to have the ability to have cellular
22 communications sent. And yet that is completely different
23 from the situation we have with the products that are
24 involved in this case, the Xbox console and Windows, where
25 the functionality is vast, far beyond any of the standards

1 that are alleged and at issue here.

2 Their own economist, Schmalensee, if you look at
3 paragraphs 2 and 3 on the handout, has agreed that you can't
4 replace this with other portfolios without assessing the
5 strengths of the products, the functions, and many other
6 things, and Donahoe admitted that he had not done that.

7 The final point with respect to the two and a quarter
8 percent, Your Honor, is, again, one, he purported to derive
9 this from Factor 1 in *Georgia-Pacific*, and to the extent one
10 is going to look to that for any kind of legal guidance, what
11 Factor 1 of *Georgia-Pacific* says is, "an established
12 royalty," and it's based on the royalties that have been
13 received, and it really puts the law to the argument that is
14 being advanced here, because no one, no one on the Motorola
15 side, not Donahoe and not the other experts, have come
16 forward and said there is an established two and a quarter
17 percent royalty for the 802.11 patents or the H.264 patents.

18 So the starting point isn't there, and that taints the
19 entire analysis that he did. It is not a reliable
20 methodology.

21 Now, the second fundamental problem with what Donahoe did
22 turns on the way in which he purported to utilize the various
23 *Georgia-Pacific*-specific factors. And, again, to the extent
24 one is going to rely on *Georgia-Pacific*, on the use of those
25 factors, not binding necessarily, but he's the one who

1 invoked it, he took us down that road, and he's got to follow
2 the rules if he's going to do that. But instead, what he did
3 was this sort of thumbs up, thumbs down, not look at this
4 factor -- actually, if you look through the factors, they
5 were all neutral or increased the royalty a little bit.

6 But what the *Whitserve* case says, and it is their sound
7 logic in that case, the *Whitserve* case says you can't do it
8 that way. You can't have a superficial recitation of the
9 factors. What the federal circuit said in that case was,
10 while mathematical precision is not required, some
11 explanation of both why and generally to what extent the
12 particular factor impacts the royalty calculation is needed.
13 That is a logical result, it is a sound result consistent
14 with the law that has been developed in that area, and I
15 certainly have every reason to believe that the Ninth Circuit
16 would follow up with a similar rule with respect to, if you
17 choose to use the *Georgia-Pacific* factor, you've got to do it
18 the right way.

19 Now, the third fundamental layer of what he did and why it
20 is not a reliable methodology is because he applied a
21 percentage royalty to the entirety of Windows and the
22 entirety of Xbox without any showing -- without any showing
23 that the Motorola patents drive demand, drive consumer demand
24 for those products.

25 Now, this gets into the entire market value rule, and,

1 again, you know, we're not going to find -- I don't think
2 we're going to find a discussion of the entire market value
3 rule in the law of the Ninth Circuit, but it is a bedrock
4 principle that has been established by the federal circuit in
5 all cases involving patent damages. And, again, I think it
6 would provide very good guidance to the Ninth Circuit in
7 trying to elucidate how one applies a royalty, what the base
8 is.

9 The logic behind the entire market rule is unassailable,
10 and that is if you have a patent, you get rewarded and you
11 get compensated for the value of your patent, but not things
12 you didn't contribute to and not things you didn't invent and
13 not other things that are in the product.

14 In this case what we know Donahoe did was simply to take
15 his two and a quarter percent and multiply it times the end
16 price of Windows and the end product price of the Xbox
17 console.

18 So how did he try to defend this? Well, if you look at
19 paragraph 10 in the handout, the argument he advanced is,
20 well, these things are important, they're important. Xbox
21 wouldn't remain competitive without them. But that is not
22 the same as being the basis for customer demand. Those two
23 things are fundamentally different.

24 And we don't have to look any further than -- again, I'm
25 citing this as persuasive precedent, the *Laser Dynamic* case

1 from the federal circuit. If you look at Slide 11, precisely
2 the same argument was advanced there. All of these that are
3 covered by these patents are important, and you wouldn't buy
4 a computer without them. But that was knocked down by the
5 Court of Appeals. And they explained here that, to name a
6 few, a high-resolution screen, responsive keyboard, fast
7 wireless network receiver, all of these things are important,
8 that consumers would be unlikely to select laptop computers
9 without them. But as they point out, proof that consumers
10 would not want a laptop computer without such features is not
11 tantamount to proof that any one of those features alone
12 drives the market for laptop computers, and that is precisely
13 what Donahoe did here.

14 One can read his expert report, one can read the reports
15 he relied on, you will not find in those reports -- you will
16 not find in those reports any basis for an assertion that the
17 Motorola patents that are allegedly essential to these
18 standards provide the basis for consumer demand of those
19 products. It's implausible, and that's probably in part the
20 reason that argument was not advanced.

21 But this notion of necessary apportionment finds support
22 not just in federal circuit case law, it finds it in the
23 Supreme Court law as well, Your Honor, that necessary
24 apportionment is required. *Aro Manufacturing*, 377 U.S. 476.

25 Now, a second argument that Donahoe advances is, well,

1 fine, maybe I've got the wrong base. You know, maybe it
2 isn't contributing to the demand for the entire Xbox or all
3 of Windows, but I'll fix that with a low rate. We can jiggle
4 the two, and we'll come out just fine.

5 But if we look at paragraph 12, what we've done in
6 paragraph 12 is to contrast what Donahoe said about jiggling
7 the rate and fixing it that way with the same argument
8 presented in *Laser Dynamics* squarely rejected by the court,
9 and, again, a perfectly logical and sound decision of the
10 federal circuit on this.

11 THE COURT: Counsel, you've used 20 of your 30
12 minutes at this time.

13 MR. PRITIKIN: All right. I'll wind up quickly, Your
14 Honor.

15 Two other reasons why -- let me just -- actually, I'll go
16 to the final reason, Your Honor, as to why this is not an
17 accepted methodology, and that is because what Donahoe did
18 was to set up and capture the holdup value of the standard
19 instead of what would be a RAND royalty for the small number
20 of Motorola patents. The court is familiar with the concept
21 of holdup. I don't need to review that again.

22 What Donahoe did was to design an analysis that would
23 maximize holdup. I mean, that's really what he did. And how
24 do we know that?

25 Well, first he used 2010 as the date of his hypothetical

1 negotiation. Now, again, he invoked *Georgia-Pacific*. But if
2 you go down that road, what *Georgia-Pacific* says is you do it
3 at the time the infringement begins. But he selected 2010.

4 By 2010, Microsoft has lots of sound cause and the
5 standards have been widely implemented. So it's not ex ante,
6 as Judge Posner had suggested at something earlier in time
7 around the adoption of the standard. It's not at the time
8 you use with *Georgia-Pacific*. It's at a time when they get
9 the greatest chokehold on Microsoft. That's holdup. And
10 there's no explanation, no rational explanation for doing
11 that, other than to maximize the holdup value.

12 Second, he valued the standard and not the patents. And
13 I've included a series of slides here, 13, 14, and 15, and
14 one can read through the language that he used there, where
15 what he's talking about in valuing these is the value of the
16 standard. 802.11 is important, H.264 is important, but what
17 he doesn't talk about is the value of the patents, which
18 would be relevant. To value the standard and the importance
19 of that, again, is holdup.

20 Now, he admitted that he didn't separate out the value of
21 the patent. He said it was too hard. Of course, again,
22 looking at the federal circuit as persuasive authority on
23 this. Then he said you don't get excused because things are
24 hard. You've got to do the hard work. And in paragraph 16
25 of the handout, we've pointed at some testimony from

1 Professor Schmalensee, their economist, who said that if you
2 do this kind of analysis where you're pointing to the
3 standard instead of the specific patents, the words he used
4 is, "it is off the mark." Well, that's exactly what it is
5 that Donahoe did here.

6 Let me see if I can pull this together, Your Honor.
7 There's a bit of a strong argument that Motorola has set up
8 that we're criticizing because of *Georgia-Pacific* and can't
9 use it. That is not the basis of our motion. That is not
10 the basis. As I said at the beginning, the *Georgia-Pacific*
11 factors is a non-exhaustive list of things that may be
12 considered. A good part of what we heard from Harrigan and
13 experts on the Microsoft side will offer will fit within one
14 or more of those *Georgia-Pacific* factors, and the court needs
15 to take those into account.

16 The problem with what they did is methodological. There
17 are fundamental methodological flaws in what he did, and it's
18 the four things that I've identified in the course of this
19 argument.

20 Once he decided that he was going to use *Georgia-Pacific*,
21 that those factors were going to provide the template in the
22 hypothetical negotiation, if you wanted to modify it, it was
23 incumbent on him or on the economist somewhere in the report
24 to say these are the modifications I made, this is the
25 economic logic behind doing them. We're off -- in many

1 respects, we're off in uncharted waters here in determining
2 what the RAND royalty is, but that's why you need a coherent
3 economic explanation for it.

4 The only way you can define how to modify the
5 *Georgia-Pacific* factors is to kind of read through the report
6 and see what he did along the way. There's really no
7 explanation for why it's done. At the end of the day, what
8 he did was go down this *Georgia-Pacific* road, take the pieces
9 of it that he thought were favorable and would generate a
10 high royalty rate, apply it to an improper base, and then he
11 just threw overboard pieces of *Georgia-Pacific* that were
12 inconvenient or that would work against him. So he discarded
13 the requirement that the licenses really have to be
14 comparable, and he's going into cell phone licenses. I mean,
15 that's one of the modifications. I don't know. There's no
16 justification for it.

17 He discarded the entire market value rule. As I said,
18 finds precedent even in the rulings of the Supreme Court
19 concept of apportionment, no basis for that. He failed to
20 apply the *Georgia-Pacific* factors in a meaningful and
21 economic way is this *Whitserve* case would require. And what
22 you're left with when you're done looking at what Donahoe did
23 is what I would call picking and choosing. Well, picking and
24 choosing is the antithesis of a reliable scientific
25 methodology, and for that reason we would ask the court to

1 exclude the testimony and opinions they plan to offer.

2 THE COURT: Thank you.

3 MR. JENNER: Your Honor, the first thing I would note
4 is, as happened with prior proceedings, these slides include
5 confidential information. Your book, Your Honor, includes
6 the confidential information. What will be on the screen
7 will be masked, just so that it's clear that we're proceeding
8 in that way.

9 This is *Daubert*, and I'll try to confine myself as much as
10 possible to *Daubert*. So let me start first by saying we have
11 a witness here, Mr. Donahoe, who is a 25-year veteran of
12 licensing, including standards essential licensing patents,
13 including working in that field for Samsung. He is probably
14 one of the most experienced licensing executives in the
15 country. His credentials, as far as I can see, are
16 unchallenged. Nobody questions that, and he has, in fact,
17 been held qualified to testify on this basis and other
18 proceedings, including the *Apple* case.

19 So this is not about his credentials. It's about
20 methodology or the application of methodology. Depending
21 upon which one of those it is, the result, I submit, is very
22 different under Ninth Circuit law.

23 As far as methodology is concerned, his methodology, which
24 I will refer to more accurately as a hypothetical bilateral
25 negotiation of which *Georgia-Pacific* applies an application,

1 mirrors the real world, unlike Microsoft's methodology.
2 Bilateral licensing in general and in standards patents has
3 been what has gone on in the real world for decades. And the
4 bilateral hypothetical negotiation in this case is intended,
5 like *Georgia-Pacific* in a damages case, to implement what
6 happens in the real world in a way that Your Honor can hope
7 to apply in establishing RAND licensing rates.

8 This kind of high-technology bilateral licensing is
9 conducted by sophisticated parties with competent counsel.
10 It considers the strength and value of the parties' competing
11 patent portfolios, it looks at the product exposure and the
12 result of risk that allows the parties bilaterally to account
13 for other considerations, including, in the RAND context,
14 whatever they want to say to each other about holdup and
15 stacking, and they ultimately craft an agreement that suits
16 their particular business needs.

17 So Mr. Donahoe's analysis uses a hypothetical recreation
18 of the real world kinds of negotiations that go on. That's
19 the real basis for this that makes it sound in a way that is
20 similar to *Georgia-Pacific*, and that's why we called it
21 modified. We, the lawyers, call it modified because this
22 isn't *Georgia-Pacific*. This is not a damages case. We are
23 not going back to the eve the infringement began. We are not
24 calculating damages in a specific case. We are licensing a
25 whole portfolio. We are licensing not only present but

1 future products. It simply isn't the same as *Georgia-Pacific*
2 applied in the damages case. That's why we, the lawyers,
3 call it modified *Georgia-Pacific*.

4 But you don't have to call it modified *Georgia-Pacific*.
5 Just call it a hypothetical bilateral negotiation in a RAND
6 context in order to achieve the goals of RAND licensing.

7 So this modified *Georgia-Pacific* --

8 THE COURT: Let me stop you there. You went back to
9 it again today. The strength of each party's patent
10 portfolios.

11 MR. JENNER: Yes.

12 THE COURT: Do you think that has anything to do with
13 the question that I have to answer starting on November 13th?

14 MR. JENNER: I believe that the strength of the two
15 parties negotiating the portfolios is what will ultimately be
16 the result in the royalty rate. It will go down as to
17 Motorola if Microsoft's offsetting portfolio is strong. It
18 will go up if Microsoft's portfolio is weak. So I think that
19 in the real world, and, therefore, I think what Your Honor
20 should consider is, this is not -- this is the discussion the
21 parties will bring to the negotiation table. They're not
22 going to talk about the thousand portfolios in MPEG LA. They
23 never would do that in a real negotiation. But they're
24 confronting each other, and they will look at what each other
25 brings to the table in order to determine what the offsets

1 are that results in the final royalty rate.

2 THE COURT: Counsel, we just have a fundamental
3 difference of opinion on this. You know, you entered
4 yourself into a contract which provides the court to set a
5 royalty rate in regards to Motorola's patents. It makes no
6 difference to me if Microsoft has zero patents or it has
7 150,000 patents in setting the royalty rate for Motorola's
8 patents. Why am I wrong on that, and why do you keep raising
9 this issue?

10 MR. JENNER: Well, Your Honor, I guess I'm swimming
11 upstream here, but I believe in a notion where both parties
12 have RAND commitments, Motorola is going to go into a
13 negotiation, and it's going to be negotiating to protect
14 itself as well. It is not going to want to give away its
15 patent rights in a real-world negotiation and be confronted
16 the next day by the adversary patents coming back at it.
17 That's not what people do in negotiations. If Your Honor is
18 going to mirror what happens in the real world, you need to
19 consider the dynamics and the facts between two parties. I
20 submit you need to consider what each party brings to the
21 table, or you're not approximating what happens in the real
22 world.

23 THE COURT: So let me ask you a very simple question.
24 Did Motorola ask me to value Microsoft's patents in these two
25 standards?

1 MR. JENNER: I guess you mean in the letters that
2 were written?

3 THE COURT: Well, in your pleadings.

4 MR. JENNER: It's not in our pleadings. We didn't
5 bring this up. Microsoft did.

6 THE COURT: You're telling me today, as you have on
7 multiple occasions, "Judge, this is a big mess. It's an 80-
8 or a 100-page document. You've got to consider all of these
9 factors." That is not what's in this case, counsel, and I
10 don't know why you keep doing this.

11 MR. JENNER: Well, I'll just try one more time, Your
12 Honor. The letters that form the predicate of Microsoft's
13 complaint are letters in which Motorola offered RAND
14 licenses, subject to cross-licenses, that was always the
15 predicate for the RAND implementation. The cross-licenses
16 were part of the bargain. There is no way on earth there
17 would have been a licensing agreement without the
18 cross-license. It never would have happened. It doesn't
19 happen in the real world, and I submit Your Honor should not
20 exclude that. You'd be going down the wrong path if you
21 exclude that. It will get you to a final rate, because in
22 considering this, we submit, and we submit that the testimony
23 and the evidence show how these factors are considered in the
24 hypothetical negotiation and result in a RAND range and a
25 RAND rate, which, in fact, are different from the starting

1 point. But you can't get there without considering both.

2 THE COURT: Counsel, I appreciate your confidence in
3 the court's Solomon-like wisdom, but that's not the issue
4 that's before me. You may have, in your responsive letter,
5 asked for a more inclusive negotiation, but your obligation
6 under those conventions is to license the Motorola patent on
7 RAND rates, and that's what's here, and if you wanted
8 something more than that, then you needed to ask me to do
9 something more than that.

10 I see the bullpen is busy handing you notes.

11 MR. JENNER: Well, they want me to make the point,
12 Your Honor, that at least the ITU letter of agreement
13 expressly is subject to reciprocity. It's right in the
14 letter of agreement for the ITU. That one is just plain
15 unambiguous as to what it is the parties would be agreeing to
16 as to RAND limitation.

17 But, Your Honor, I know we disagree on this. I don't want
18 this to be an entirety of the *Daubert*.

19 THE COURT: So why don't you move on.

20 MR. JENNER: Okay. Turning to Slide 3, this is some
21 of the law that we submit, unlike multilateral negotiations,
22 the courts have considered the possibility of implementing
23 FRAND under a framework, and the framework they talk about
24 in the *Broadcom* case, it's *Georgia-Pacific*, and in the *ESS*
25 district court case it was *Georgia-Pacific*. Nobody had to go

1 all the way and determine RAND licensing rates, but both of
2 these courts recognized that this was the framework that made
3 sense to consider.

4 Likewise on Slide 5, to the extent people pay attention to
5 the commentators, the commentators have said that
6 *Georgia-Pacific* is a sensible framework and provides a useful
7 starting point and factors that would be directly applicable
8 to FRAND.

9 On page 5, which I just overshot -- on Slide 5, Your
10 Honor, we list some of the case-bound papers on this. You
11 heard earlier about Microsoft's June 11 letter to the FTC.
12 After the litigation began, Microsoft acknowledged to the FTC
13 that RAND policies help enable bilateral negotiations.
14 Microsoft's *Daubert* surreply in a different litigation
15 recognized *Broadcom* and *ESS Technologies* and pointed out that
16 they point to a relationship between RAND and
17 *Georgia-Pacific*. And the experts Simcoe and Lynde in this
18 case both recognized that applying the factors of
19 *Georgia-Pacific* could get you to RAND. So I submit the
20 methodology, Your Honor, is well recognized by courts,
21 commentators, and Microsoft itself. It's the right
22 methodology so that the question we're coming to under
23 *Daubert* is whether the application of the methodology is so
24 flawed and so off the mark that Your Honor shouldn't hear it
25 subject to cross-examination, then I submit the answer is no.

1 You have a question?

2 THE COURT: I was going to direct you to -- because
3 you're going to use your time. Let's not argue about the
4 applicability of *Georgia-Pacific*. That's a legal issue that
5 I think the court is bound on where it goes on that.

6 Let's talk about Mr. Donahoe, because I have some very
7 serious concerns, starting with his assumption of the 2.25
8 percent royalty. So I'd like you to use your time wisely
9 here.

10 MR. JENNER: Okay. Let's look at that. There's a
11 little bit of that on Slide 5 under the point of his reliance
12 on substantial evidence.

13 He relies on a lot of licensing agreements as a way to get
14 there. Counsel is wrong in the way his expert reports X that
15 out. And if you look at page -- for the record, page 35 and
16 following in his expert report, what you're going to see is
17 that Donahoe actually relies on a subset of about seven
18 licensing agreements in order to look at what the starting
19 point should be. The other agreements are more of a general
20 guide for how the negotiations are conducted by Motorola,
21 what kinds of other things Your Honor might consider, like
22 carve-outs and caps and suspension clauses and that sort of
23 thing.

24 But the fundamental seven agreements are ones which don't
25 pull out single patents. They license the entirety of the

1 802.11, H.264 portfolio, or both, and two of those agreements
2 clearly are the best comparables. They're right on the
3 money. One of them is the VTech agreement in which nothing
4 is licensed for essential patents except 802.11 and H.264.
5 And in that agreement, it is the licensee who approached
6 Motorola looking for the license proposing rates, which I'll
7 show you on another slide, which were substantial rates and
8 ultimately wound up being negotiated to the rate that
9 Motorola seeks.

10 There's another licensee, which I guess I'm not supposed
11 to name. It's one of the same seven which also negotiated a
12 license where they had substantial value to give back to
13 Motorola in the form of patents. The royalty rate was
14 somewhat lower. But they have products that are only
15 utilized in the 802.11 and H.264 portfolios. In those
16 products where they're paying the full royalty, they're right
17 on the money, they are comparables. There are lots of cases
18 that looked at only one or two comparables as the basis to
19 find the starting point, in contrast to Microsoft, which has
20 no starting point at all.

21 THE COURT: Well, your starting point is deeply
22 troublesome to me, because what I got out of the report,
23 starting on page 34, it says, "The information establishes
24 that Motorola typically opens negotiations by offering rates
25 between 1.7 and 2.25."

1 You know, that's an assumption. That's, you know, someone
2 told him this, you know, this is where to start, and it
3 impacts his entire analysis.

4 MR. JENNER: Well, somebody told him where to start.
5 Your Honor, those are the facts that he looked at and
6 concluded that it was fair to start there.

7 THE COURT: What you just told me is he looked --
8 first off, I assume that you agree with Mr. Batchelder, who
9 threw all your cellular licenses under the bus this morning;
10 that it was a different industry, a different set of patents,
11 different convention. They're gone.

12 So let's talk about the specific question that we're
13 looking at, which is the 802.11 and the H.264, and you're
14 telling me now you've got two licenses that cover those.

15 MR. JENNER: Two licenses that are squarely on point.

16 THE COURT: And one of those is on page --

17 MR. JENNER: If Your Honor would turn to Slide 16.

18 THE COURT: I'm actually in his report.

19 MR. JENNER: Oh. Sorry.

20 THE COURT: It would be paragraph 82, the VTech
21 Communications. That's one of your two that we're looking
22 at.

23 MR. JENNER: Yes, it is.

24 THE COURT: Okay. And by paragraph, since you don't
25 want to mention the name, what is the other one he refers to?

1 MR. JENNER: Um --

2 THE COURT: Counsel, where I'm going with this -- you
3 have to read and listen at the same time. Where I'm going
4 with this is, it strikes me that what you're proposing is
5 basically what the federal circuits tossed, which is, Hey, we
6 all start at 25 percent, that's our royalty. Whatever -- it
7 doesn't matter what the patent is, it doesn't matter what the
8 price is, it doesn't matter what the contribution is, we
9 start at 25 percent. The federal circuit rang the bell on
10 that.

11 MR. JENNER: Absolutely not the same thing, Your
12 Honor. It's not the same thing at all.

13 You're talking about the so-called rule of thumb, where in
14 the *Uniloc* case and in some cases that follow that, there's
15 an unpublished decision in the *Oracle* litigation that looked
16 at another rule of thumb that had a fancy name.

17 The court looked at a situation that had nothing to do
18 with being tethered to real-world licensing agreements. The
19 experts came in and said, "Oh, today is a sunny day. We're
20 going to take 25 percent of profit and use that as a starting
21 point." Untethered to licensing agreements, untethered to
22 Factor 1 of *Georgia-Pacific*. These licensing agreements are
23 completely tethered to *Georgia-Pacific*, and they are the
24 closest comparables in the case. They're necessarily the
25 best starting point for Your Honor to use in trying to figure

1 out what RAND would be.

2 THE COURT: Well, I mean, I think the response to
3 that -- I'm enjoying the discussion -- is that it's
4 untethered to reality, because, you know, you've taken it and
5 you're now applying it to a different situation and saying
6 it's the same. The contribution of the Motorola patent to
7 the product seems untouched by your analysis.

8 MR. JENNER: The contribution of the patents to the
9 products is discussed elsewhere in other factors by Donahoe.
10 He considered some of those factors -- and by the way, I want
11 to point out this is very different from --

12 THE COURT: Do you have that paragraph?

13 MR. JENNER: It starts at paragraph 68. I want to
14 point out, first of all, that the product -- the patent
15 application to the products is discussed over a number of the
16 factors on pages and pages by Mr. Donahoe, where he either
17 finds no effect or he finds in some cases it would have a
18 tendency to drive the royalty upward. That is specifically
19 criticized by counsel in the *Whitserve* case, and I don't want
20 to leave that untouched, because in the *Whitserve* case, what
21 really happened, if you look at Footnote 15 in *Whitserve*,
22 which is at page 35 of the slip opinion, you'll find out what
23 the expert in that case did was to discuss and analyze
24 nothing. There was one question and answer given as an
25 example where the witness was questioned about two of the

1 factors, 9 and 13, and then he answered, "Well, here's a
2 chart that shows advantages. I find they would support a
3 higher royalty rate."

4 What the *Whitserve* court was criticizing is not that you
5 can have factors driven up or down, but rather that you have
6 to have some explanation of why you reached the conclusion.

7 There are cases that we cite in these slides, which I may
8 or may not be able to come to, where you'll see federal
9 district courts have, in fact, done this as a matter of
10 routine. Why? There's no other way to do it. We're looking
11 at lots of factors where you're trying to talk about whether
12 or not a patent is valuable. Does Microsoft really want you
13 to think there is some algorithm that you type that into, and
14 the algorithm tells you, okay, increase the royalty rate by
15 .2? You can't have that kind of precision.

16 THE COURT: Don't set up the straw man. Stay with
17 your expert --

18 MR. JENNER: Okay -- look at --

19 THE COURT: Don't interrupt me, sir. I don't
20 interrupt you.

21 What I got out of Mr. Donahoe was he said, "I rely on the
22 opinions of technical witnesses who have discussed the
23 importance of Motorola's standard essential patents to the
24 standard."

25 Where in my paragraph is that?

1 MR. JENNER: I'm going to need some help with that.
2 It's in the following factors where he essentially discusses
3 some of the factors between Factors 3 and 13. It occurs
4 between pages, roughly, 40 and page, I'm going to say, 75 of
5 the report, where he is discussing the patents, the scope of
6 the patents, how the patents compare to the standard. I'm
7 sorry to say, but also how the parties' patents compare with
8 each other. And he gets all of that information from the
9 technical witnesses who will provide that background. So he
10 is not the technologist. He doesn't purport to be a person
11 who is able to look at these complicated patents, but he is
12 relying on the output of the other experts as input for him
13 as the negotiator, and that's what happens in the real world.
14 That's what teams do.

15 THE COURT: Will you agree with me, then, that if I
16 find that he is relying on opinions in regards to the value
17 of the standards as opposed to the value of the
18 industry-essential patent, that I should disregard his
19 report?

20 MR. JENNER: No, I can't rely on that entirely, but I
21 can think of at least two ways in which that wouldn't be
22 fair, and I think he probably does this in two ways. One is,
23 where there are so many patents involved, that it is
24 unrealistic and impractical to evaluate 40 individual
25 patents. He likely relies on the standard as a proxy for

1 what the patents cover, and I don't think there's anything
2 unfair about that at all.

3 If he then goes on and takes the standard and tells you
4 you should increase the royalty rate because of the standard,
5 that could be a problem, but he doesn't do that, either. He
6 looks at the standard as a proxy for what the patents cover,
7 and I think in three or four places he says that would tend
8 to move the royalty upward, but, in fact, he doesn't do that.
9 He doesn't do that. There is no increase for the value of
10 the standard in his calculations. There's no possibility of
11 holdup having been built into what counsel refers to because
12 he said he didn't increase the royalty rate for any of that.

13 THE COURT: He found lots of things that increased
14 the royalty rate --

15 MR. JENNER: But he didn't bump the royalty rate up.
16 He said, "I'm not going higher because Motorola doesn't go
17 higher," and he didn't. He stayed true to his word.

18 THE COURT: All right. Point me to where in his
19 analysis did he explain how a portion -- which components of
20 Microsoft's products were patented and which portions were
21 unpatented.

22 MR. JENNER: The closest I think I can come to that
23 is I think it's in the expert reports of Williams and Drabik,
24 because they are technologists who do that. They provide
25 that information. There's no motion against them because

1 they, in fact, do an extremely thorough, probably 100-page
2 job of marching through the patents and exploring the
3 analysis. They go through what the patents are, patent by
4 patent, what they cover, they talk about alternatives to the
5 extent you can talk about alternatives. That's the job of
6 the technical experts, and they're the ones who do that.
7 That isn't the role of Donahoe.

8 THE COURT: Fine, but he then has to say, "I relied
9 on their reports in some manner to adjust as a consideration
10 under the *Georgia-Pacific* factors." Where did he do that?

11 MR. JENNER: I'll give one example at page 58,
12 paragraph 113, he expressly relies on Dansky. On page 60 he
13 expressly relies on input from Dansky. All I can do here is
14 turn pages to try and find examples. My co-counsel was
15 trying to pass me some examples, which I'll hurriedly try to
16 find. There's another example, Your Honor. Paragraph 134,
17 he expressly relies on his review of the Williams and Dansky
18 reports. Paragraph 142, he expressly relies on Drabik. 141,
19 he expressly relies on Drabik and Dansky. Paragraph 143,
20 expressly on Drabik and Dansky. His report relies throughout
21 on the input of the other experts who are competent to render
22 expert opinions in their fields. He is the licensing expert.
23 He's taking their inputs. And that's the way it ought to be.

24 THE COURT: You're going to run out of time, so let
25 me waste some more of it.

1 You've got what seems to be an inconsistency or a
2 contradiction. You're urging on the court a *Georgia-Pacific*
3 analysis modified, however you wanted to describe it.
4 However, you then say, "Judge, pay no attention to the entire
5 market value rule because it's inapplicable." How can you
6 reconcile because of the acceptance of the entire market
7 value of *Georgia-Pacific*? How can you reconcile that?

8 MR. JENNER: I'll go through quickly. You wanted
9 important input on what the Ninth Circuit has to say, and I
10 wanted to point out on Slide 8 that all of these four attacks
11 by counsel go to the application of methodology to the
12 evidence, and the Ninth Circuit at the bottom of Slide 8 has
13 said, in *Kennedy v. Collagen Corporation*, that faults, if
14 there are faults, in the use of a particular methodology, go
15 to weight. So I'll give you my conclusion now just so I
16 don't run out of time. That all of the attacks that counsel
17 chooses to apply to the methodologies implemented by
18 Mr. Donahoe should go to weight, if anything, and Your Honor
19 should deny the motion for that reason.

20 But let me go to the entire market value rule. The entire
21 market value rule, as much as counsel won't want to accept
22 it, is and always has been a tool implemented in damages
23 analyses. Counsel placed heavy reliance on the *Laser*
24 *Dynamics* case, and he had a picture he put up from *Laser*
25 *Dynamics*, which is his paragraph 11. It starts out by

1 saying, "We reaffirm that in any case involving
2 multicomponent products, patentees may not calculate damages
3 based on sales of the end product." Well, why is that
4 different? The entire market value rule is applied in the
5 determination of the value of an injury in a patent
6 infringement case. It doesn't exist in the real world, and
7 it never has.

8 Your Honor is being asked to throw out hundreds of years
9 of licensing negotiations, where parties license their
10 patents on the basis of end products.

11 If you look at Slide 21, for starters, Slide 21 shows,
12 first of all, that industry, now and forever, has always used
13 end product prices as a royalty base. Why? Because it's
14 easily observable, it's calculable, you can make royalty
15 reports, it makes it's easier to account for how you're going
16 to pay for future products.

17 They don't have that in *Laser Dynamics*. They're not
18 litigating damages on future products. They've got a product
19 in front of them, they're figuring out it infringed, and
20 they're calculating what the damage should be for it.

21 It's different from standard licensing negotiations that
22 parties conduct in the real world. Agreements often do this
23 in order to provide a patent piece for entire present and
24 future product lines, it enables royalty rates to adjust down
25 the road as prices change for products where you're not

1 fighting about those products.

2 Motorola has always done this. I mentioned 28 out of 33
3 licenses are based on net product price. Microsoft does it
4 on its own licenses. Once of the standards here at the
5 bottom of Slide 21, the IEEE expressly provides for using
6 percent of product price as the basis for the RAND agreement.

7 So everybody out there does this in the normal course in
8 the real world.

9 Slide 22, a reputable licensing treatise recognizes that
10 it is quite common, if not the most common, for royalties in
11 license negotiations to be predicated on the end product and
12 the end product price.

13 In the *Lucent v. Gateway* case, even though they were
14 calculating damages and had to do what they had to do,
15 including the entire market value rule, the court
16 acknowledged that sophisticated parties routinely enter into
17 licensing agreements that base the value of the inventions as
18 a percentage of the commercial product sale price.

19 And then other district courts have gone even farther. In
20 damages cases themselves where the parties have a history of
21 having crafted licensing agreements based on the end product
22 price, the courts say even that's different from the entire
23 market value rule, because here the parties have a practice
24 of licensing on the basis of the end product price, just like
25 Motorola and Microsoft do.

1 And in the *Boeing*, *Mondis*, and *Riles* cases, they said
2 never mind the entire market value rule. The product prices
3 apply because that's what the parties' licensing history has
4 been.

5 So I submit, Your Honor, the only fair way to look at this
6 on Slide 25 is that the entire fair market rule is a creature
7 that the federal circuit fairly applies -- one can squabble
8 with that, I suppose -- but fairly apply in calculating
9 damages, which is simply a different thing from the ordinary
10 arm's length licensing negotiations that go on every day,
11 where parties can and should be entitled to contract on
12 whatever basis they want, and if they find it convenient as a
13 matter of accounting to contract on the basis of the end
14 product price, that doesn't violate the entire market value
15 rule. And Microsoft's own expert on valuation here,
16 Dr. Lynde, agreed that the royalty can be RAND if it's not
17 calculated on the entire market value rule.

18 Your Honor needs to draw, I submit, a distinction between
19 damages --

20 THE COURT: Let me stop you. If you keep talking,
21 you're not going to have any time to talk about your survey
22 expert.

23 MR. JENNER: All right. Your Honor, I'm done, then,
24 unless you have any questions.

25 I submit that on the basis of the Ninth Circuit's own law,

1 these are criticisms of which I can rebut every single one of
2 them. They're unfair and unfounded as to Donahoe, but, in
3 fact, they go to the application of his methodology. They
4 are not a basis in the Ninth Circuit or I think any place
5 else for excluding a witness. At most, they go to weight,
6 and Your Honor ought to hear the witness.

7 THE COURT: Other than in Judge Posner's courtroom.

8 MR. JENNER: Well, Judge Posner, he got it wrong,
9 too, when he thinks that incremental value should be
10 calculated in multi-patent cases. It's one thing in a
11 damages case like he had to talk about incremental value for
12 one patent and then throw the damages out. It's another
13 thing where you, Your Honor, have 40, 50, 60 patents that are
14 10 or 20 years old, how are you going to calculate
15 incremental value? Even Microsoft didn't try to do that. He
16 got it wrong when he says you can apply that in a case like
17 this. It just doesn't work, and nobody in the real world
18 does it.

19 I'm done.

20 THE COURT: I'm delighted to say Microsoft and
21 Motorola --

22 MR. JENNER: I'm happy to be quoted on that, Your
23 Honor. Thank you.

24 THE COURT: Mr. Pritikin?

25 MR. PRITIKIN: Yes, sir. I'd like to respond to just

1 a couple of points very briefly.

2 THE COURT: All right. You're going to exhaust your
3 time on survey.

4 MR. PRITIKIN: I thought I reserved time.

5 THE COURT: You have four minutes. You can use
6 two/two.

7 MR. PRITIKIN: I'll try to use a minute, if I can,
8 Your Honor, with respect to the licensing.

9 THE COURT: I'll tell you, by the way, survey is not
10 that critical to me. I think I understand that issue. I get
11 it frequently. I wouldn't spend a lot of time on it.

12 MR. PRITIKIN: All right. With respect to the
13 licensing agreements, if you look at Slide 12 that Mr. Jenner
14 used, we're down now to six of them, and I would direct the
15 court specifically to the expert report of Mr. Donahoe where
16 he talks about those, and I want to keep the names -- I'll
17 try to protect the confidentiality of this.

18 But the Option NV is in paragraph 78, the Samsung is in
19 79, Kodak is in 80, Ericsson was in 81, RIM is in 68, and
20 Nokia is in paragraph 64 and the ones that follow.

21 What you'll see if you actually go back and look at those
22 is that for a number of those, Donahoe says specifically he's
23 not placing reliance on those agreements. That is in black
24 and white in the Donahoe report, and I would invite the court
25 to go back and look at those paragraphs to see what he

1 actually said about it.

2 With respect to the paragraph 68 company, there are really
3 two of them left that they're relying on, I would invite the
4 court to take a look at paragraphs 22 and 23 of the Lynde
5 report, in which Motorola attached as Exhibit 46 in their
6 opposition, and that has additional facts relating to that
7 agreement that make it abundantly clear that it is not and
8 cannot be a comparable. Pages, excuse me, 22 to 23 of the
9 Lynde report.

10 Just a couple of other quick points, Your Honor. You
11 asked Mr. Jenner whether or not they were valuing the
12 standard or the patents. Again, I invite the court to look
13 at the handout that I provided.

14 There's text there from the Donahoe report, and all you
15 have to do is read paragraphs 113 through 120 of the Donahoe
16 report where he's kind of pulling it together on 802.11 and
17 H.264, and he talks again and again about the standard and
18 why the standard is important in the Microsoft patents.

19 Now, we heard a new argument a few minutes ago, and the
20 reason that it's okay to do that is to look at the standard.
21 You asked Mr. Jenner the question, he said there was so many
22 patents. Well, that isn't true, either. All you have to do
23 is look at their findings of fact, and we're down to just
24 nine 802.11 patents that are supposedly implicated by Xbox.
25 And in H.2064, I think it's some 15 patents, but eight of

1 those are all of the same specification, essentially the same
2 thing that's in those patents. So that argument just doesn't
3 hold water, that there are too many patents for them to do
4 the hard work that they needed to do.

5 The last point on the entire market value rule, Your
6 Honor, we ought to stand back and look at this argument
7 that's being advanced here. They're turning it on its head.
8 The entire market value rule was developed as a protection,
9 as a safeguard to be sure the patent owner isn't overclaiming
10 and getting things that he didn't deserve, and that's why the
11 bedrock principle has been established in damages.

12 What Motorola is telling us is that in the case of a
13 standard central patent, where you're under an obligation to
14 license it in reasonable and nondiscriminatory terms, all
15 bets are off, you get more. You can do things once you've
16 declared your central patent is RAND and undertaken the
17 solemn commitment, now you're free of all the shackles that
18 would otherwise be imposed on you to protect you from
19 overclaiming. It's backwards. It makes no sense.

20 The entire market value rule finds its authority in
21 Supreme Court precedent, in the *Garretson v. Clark* case and
22 in the *Aro* case that I cited before.

23 Unless the court has questions, I'm going to give
24 Mr. Harrigan a couple of minutes to talk about survey.

25 THE COURT: Okay.

1 MR. HARRIGAN: I'll be very quick, Your Honor.

2 Your Honor, the notebook is going to get there in time for
3 you to use it.

4 Here's the bottom line: There's a lot of pieces of paper
5 in here, but they boil down to and they highlight some things
6 that are not highlighted in the brief.

7 The point is that this survey was used to determine how
8 important these two technologies are. Among the defects in
9 the survey, the key one is that the people who did -- who did
10 not connect to the Internet, who owned an Xbox but did not
11 connect to the Internet with it, were kicked out of the
12 survey. If they checked the box that they didn't connect to
13 the Internet, they weren't included in the sample. So the
14 measuring of connecting to the Internet by excluding the
15 people who don't connect to the Internet, and then the
16 conclusion is, for example, Mr. Dansky says about 45 percent
17 of the Xbox customers have used the 802.11 adapter to connect
18 to the Internet, that excludes the people who didn't connect
19 to the Internet. So the common denominator in the fraction
20 is way too low, it's way too small, and the percentage goes
21 way up.

22 And those rates -- and there are several examples of how
23 that affects that -- those rates are the basis for part of
24 Mr. Donahoe's testimony and a good part of Mr. Dansky's
25 evaluation.

1 The other -- and you can see this is all laid out in these
2 slides for your perusal. The other basic problem is that
3 people were asked to whether -- to what extent they'd watch
4 MBAFF video. They had no idea what it meant. And like
5 Motorola's own witnesses agree, there's no way to tell unless
6 you get out a machine that measures it, and presumably none
7 of these people did that.

8 Thank you, Your Honor.

9 THE COURT: Ms. Hoang, you have about the same amount
10 of time.

11 MS. HOANG: Okay. Thank you, Your Honor.

12 I guess it's worth noting right off the bat that the first
13 argument that Mr. Harrigan made was a new one. It was not in
14 any of their briefings or in their 28-page expert declaration
15 to this court of the *Daubert* motion, the discussion about
16 exclusion of Xbox users who were not connected to the
17 Internet.

18 What I would say to that, Your Honor, is that the surveys
19 were designed to measure usage by Xbox owners and Xbox users
20 and were designed to measure the valuation or the relative
21 valuation by these Xbox owners and Xbox users of particular
22 features.

23 Dr. Sukumar's methodology used closely to the
24 fundamentally accepted principles for survey research and
25 survey conducting. He references and adheres to the

1 *Reference Guide on Survey Research*, which is maintained by
2 the Federal Judicial Center. That is recognized by
3 Microsoft's experts as well. The sample set that he used, we
4 would submit, Your Honor, is reliable because it, as I
5 mentioned, adheres to all these various principles, and I'm
6 hoping that our opposition to their *Daubert* papers lays that
7 out pretty well.

8 I will touch on the MBAFF situation in just one moment.
9 Your Honor, they're overlaying an impossible and really
10 irrelevant standard to MBAFF. Technical experts dealing with
11 infringement issues must uphold a much, much more rigorous
12 standard. They have to do claim construction, they have to
13 apply claims, and they have to map them, and, of course, they
14 need software tools and other things to understand whether
15 MBAFF, as it is set forth in a particular patent claim,
16 exists.

17 This is a survey that simply asks Xbox users and Xbox
18 owners, do you know what you're watching? If you don't
19 click, the third button that says "I'm not sure." If you do,
20 then presumably you will click the button that says "MBAFF."
21 That's all it's meant to do. It doesn't say you must know
22 technically what MBAFF is, you must be able to define it, you
23 must be able to measure it using a software tool. This is
24 nothing more than a simple question that says do you have --
25 are you aware of what you're watching in terms of videos on

1 your Xbox console?

2 THE COURT: Would you read me the actual question?

3 MS. HOANG: Yes. It's the very first slide in my
4 deck. It's Slide No. 2. The question says, "Please select
5 the types of video content you have used on your Xbox console
6 connected to your TV." There's only three choices. One is
7 "MBAFF," and the acronym is spelled out, one is
8 "progressive," and one is "not sure." There's nothing
9 implied in the question that would force someone to answer
10 "MBAFF" if they didn't understand what it was. It is not a
11 complicated question. It's not long. There aren't very many
12 choices to make. And there's a clear and clean opt-out that,
13 according to the survey principles, vastly reduces any
14 potential confusion or false positives, and that's present
15 and available for any survey respondent to select, and as it
16 so happens, 84 percent of the survey respondents did not pick
17 MBAFF. A very small percentage of people were able to
18 identify it and select it, and that's all it was designed to
19 measure. That's it.

20 THE COURT: Counsel, was there a question in there
21 about how much they had to drink during the football game
22 before answering this question?

23 MS. HOANG: I'm constantly surprised about what
24 gamers know and don't know about video technology, if that's
25 where their interest lies.

1 THE COURT: Counsel, thank you.

2 MS. HOANG: Thank you.

3 THE COURT: We'll take this matter under advisement.
4 I thank you for a spirited and informative session today. I
5 believe I see you next on the 29th for the pretrial
6 conference, and we'll look forward to that.

7 MR. PALUMBO: Your Honor, we have a lot of boxes to
8 pick up. Will the courtroom be open after the noon hour so
9 we can have someone come and get it?

10 THE COURT: Yes.

11 MR. PALUMBO: And with respect to issue of closing
12 the courtroom during trial, if there's any information we
13 believe that meets the Ninth Circuit's compelling interest
14 standard, we'll file the appropriate motion with respect to
15 our information.

16 The question I have is, there may be third parties who
17 seem to protect their licensing information. Is it the
18 court's preference that those third parties simply file a
19 motion, or seek the court's permission before filing a
20 motion?

21 THE COURT: They can file a motion.

22 MR. PALUMBO: Thank you, Your Honor.

23 THE COURT: Anything further? Then we'll be in
24 recess. Thank you, counsel.

(THE PROCEEDINGS CONCLUDED.)

C E R T I F I C A T E

I, Nancy L. Bauer, CCR, RPR, Court Reporter for the United States District Court in the Western District of Washington at Seattle, do hereby certify that I was present in court during the foregoing matter and reported said proceedings stenographically.

I further certify that thereafter, I have caused said stenographic notes to be transcribed under my direction and that the foregoing pages are a true and accurate transcription to the best of my ability.

Dated this 23rd day of October 2012.

/S/ Nancy L. Bauer

Nancy L. Bauer, CCR, RPR
Official Court Reporter